

## Adjusting to Copper Prices

United States Influence on the International Monetary Fund and the World Bank  
Conditionality: the case of Zambia in 1964–1991

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<p>Tiivistelmä – Referat – Abstract</p> <p>Tutkin tässä työssä Kansainvälisen valuuttarahaston ja Maailmanpankin lainaohjelmia Sambiassa vuosina 1964–1991. Monen muun afrikkalaisen valtion tavoin Sambia ajautui 1970-luvulta lähtien tukalaan velkakierteeseen, ja sen talous tuli riippuvaiseksi kansainvälisten rahoituslaitosten myöntämistä lainoista. Maailmanlaajuisen velkakriisin puhkeamisen jälkeen Kansainvälinen valuuttarahasto ja Maailmanpankki ajoivat velkaantuneissa kehitysmaissa läpi yksityiskohtaisia rakennesopeutusohjelmia. Järjestöt tukivat ohjelmien toteutusta lainoilla, jotka sisälsivät alati lisääntyviä määriä taloudellisia ehtoja. 1980-luvun lopulla rakennesopeutuksen tavoite oli kehittyvien kansantalouksien rakenteiden kokonaisvaltainen uudistaminen. Tätä agenda taustoitti järjestöjen tiivis yhteistyö Yhdysvaltojen republikaanisen hallituksen kanssa sekä uusliberaalin talousideologian läpimurto.</p> <p>Afrikan rakennesopeutusohjelmat ovat monitahoinen ja kiistelty tutkimusaihe. Tutkimukseni tavoite on tarjota tasapuolinen ja aiheen moniäänisyyden huomioon ottava analyysi Sambia rakennesopeutusohjelmista. Tämän vuoksi olen valinnut työn teoreettiseksi lähtökohdaksi relationaalisen lähestymistavan, jossa tarkastelen tutkimusaihetta kahdesta eri perspektiivistä, fokuksen kiinnittyessä näkökulmien väliseen suhteeseen. Tutkielman toisessa luvussa keskityn ehdollisten lainaohjelmien kehitykseen sekä Yhdysvaltojen hallituksen vaikutukseen tässä prosessissa. Sen lisäksi analysoin uusliberaalin talousideologian leviämistä rahoitusjärjestöihin. Kolmas luku on kronologinen kuvaus Sambia talouden kehityksestä itsenäistymisen jälkeen, ja käyn luvussa läpi myös tärkeimmät poliittiset käänneet tältä ajalta. Ennen kaikkea pyrin kolmannessa luvussa heijastamaan edellisen luvun päätelmiä Sambia tapaukseen. Sambia taloudellinen menestys on ollut riippuvaista kuparin tuotannosta ja maa ei toipunut raaka-aineen hinnan romahduksesta 1970-luvun puolivälissä.</p> <p>Työn pääasiallisina lähteinä käytän Kansainvälisen valuuttarahaston ja Maailmanpankin asiakirjoja, jotka ovat vapaasti saatavilla organisaatioiden verkkoarkistoissa. Rakennesopeutusohjelmia on tutkittu melko paljon ja sovelletaan relevanttia tutkimuskirjallisuutta etenkin toisessa luvussa. Tutkimus osoittaa, että suurin syy Sambia taloudellisen alamäkeen löytyy maan autoritäärisen hallinnon tekemistä virheistä sekä laajalle levinneestä korruptiosta. Kansainvälisten rahoitusjärjestöjen kyvykkyyden Sambia tilanteen auttamisessa voi silti kyseenalaistaa, ja järjestöjen toiminta osoittautuu jossain määrin epäjohdonmukaiseksi. Rakennesopeutusohjelmien kehitys kansainvälisissä rahoitusjärjestöissä oli vaiherikas ja hidas prosessi. Johtopäätöksissä korostuu tämän prosessin kokonaisvaltaisen kartoittamisen merkitys yksittäisten tapausten tutkimisessa.</p>		
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# 1. Introduction

## 1.1 The Lost Decades

The 1980s and 1990s have been labelled the “lost decades” of Africa. Following the initially promising economic growth of the post-independence years, most African countries were hit hard by the oil crisis in 1973 and the subsequent stagnation of the world economy. In many parts of the continent, the result was a deep debt crisis, which paralysed economies for many years to come. The consequences of the mounting debt were devastating both economically and socially. From 1981 to 1996 nearly half of all African nations “experienced significant episodes of violent conflict between government and opposition groups”<sup>1</sup>. Although ethnic atrocities sparked many of these conflicts, one can hardly downplay the significance of poverty and economic woes in generating social unrest. While economic growth has picked up again in the new millennia, Africa remains the poorest continent in the world.

The history of independent Zambia illustrates vividly the general trajectory of African economic development. Formerly known as Northern Rhodesia, the British protectorate gained independence in 1964. The republic’s first president, Kenneth Kaunda, established a semi-authoritarian socialist one-party state and reigned for over 25 years. Rich in natural resources, Zambia rapidly emerged as one of the most prosperous states in Africa. However, the Zambian economy was too heavily reliant on its mining industry and economic troubles commenced when copper prices plummeted in 1975. As revenues from the mining sector dropped, the state was unable to sustain growth and a severe economic downturn followed. The Zambian government turned to the international financial institutions (IFIs)<sup>2</sup> and other creditors for aid in the form of debt. Despite receiving substantial loans, Zambia was unable to recover and a large part of the population was

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<sup>1</sup> Goldsmith 2001, 128.

<sup>2</sup> This abbreviation refers to the International Monetary Fund and the World Bank. When referring to just one of these institutions I will employ the commonly used terms: The Fund and the Bank.

dragged into poverty. By the 1990s, the real gross domestic product (GDP) per capita had nearly halved since independence<sup>3</sup>.

The turbulent 1970s brought an end to the Bretton Woods system<sup>4</sup> that had set the rules for the global economy since World War II. The upheavals of the decade also transformed the role of the IFIs, created in Bretton Woods. Originally, the International Monetary Fund's purpose was to oversee fixed currency exchange rates between countries and to provide short-term capital to aid balance of payments<sup>5</sup> problems. The World Bank was operating with a mandate of granting loans to poor countries in order to bolster development. These loans were often tied to projects for building infrastructure in the developing states.

In the 1980s the Fund and the Bank started issuing loans which were characterised by heavy conditionality. From the 1950s onwards, conditions had been attached to loans but they were mostly in the form of macroeconomic policy guidelines. Three decades later, very specific economic conditions and benchmarks accompanied the loans. In 1979, the conditional loan programs, catered to serve the needs of developing countries in financial distress, were named structural adjustment programs (SAPs). There were several reasons behind the transformation of the financial institutions. One can argue that the economists working in the IFIs – most of whom had studied in Western universities – were simply doing their best to help poor countries in debt problems and thus decided to develop their lending strategies. To some extent this is certainly true, but the picture becomes more complex if one considers that the underlying goal of the IFIs is to ensure their return of capital. After all, their aid was in the form of loans.

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<sup>3</sup> World Bank Open Data, 13 March 2019. *GDP per capita (constant 2010 US\$): Zambia*. The economic hardships were aggravated in Zambia by rapid population growth.

<sup>4</sup> The Bretton Woods system was a pioneering experiment because for the first time in history independent states created a regulatory order for international monetary relations. The Fund had an essential role within the system as an interventionist organ. The Bretton Woods system can broadly be described as a combination of Keynesian economic control and a liberal attitude towards trade. The latter was endorsed because high tariffs and other protective measures were seen as significant reasons in making the Great Depression so devastating in the 1930s. However, state control was also encouraged since Keynesian economics relied on the state's ability to stimulate domestic demand and manage unemployment.

<sup>5</sup> Balance of payments refers to the sum of transactions of a particular state with the rest of the world. The revenues of a state consist for example of exports, foreign investment and foreign debt, whereas imports and the payments of debt can be counted as state expenses. Under the fixed exchange rate system of the Bretton Woods era, this meant that a deficit in the balance of payments would deplete the central bank's reserves of foreign currency. This in turn was followed by downward pressure on the value of the domestic currency and thus a heightened risk of an inflationary spiral. (Ylönen 2012, 22.)

One can also view the birth of the SAPs as a manifestation of a paradigmatic shift in the field of economics. The 1970s witnessed, not only the crumbling of the world economy, but also the downfall of Keynesian economics, dominant since World War II. The assault on Keynesian economics was led by Milton Friedman and his associates from the so-called Chicago school of economics. They rekindled the classical idea that a simple set of abstract laws governed economics. State control was to be minimised and free markets along with unrestricted movement of capital promoted. By the 1980s, these neoliberal ideals dictated economic policies in most parts of the Western world with Ronald Reagan's administration (1981–1989) in the United States (US), as well as Margaret Thatcher's government (1979–1990) in the United Kingdom (UK), endorsing them. The proliferation of neoliberal economic policies was epitomised in the birth of the Washington Consensus<sup>6</sup>, a 10-point list of economic policies targeted to the developing countries and designed together by the IFIs and the US Treasury Department. Thus, the imprint of neoliberalism was clearly visible in the SAPs. In order to receive loans, strict austerity and balanced budgets were required. In addition, conditions often included privatisation of state-owned companies, cutting corporate taxes, letting in foreign capital and liberalising trade.

## **1.2 Research Questions and Methods**

The debt crisis and IFI's policies in Africa have been researched at length. In my opinion, however, too many of the studies follow a rather distinct dogmatic perspective in doing so. Quite commonly, the debt crisis and consequent painful adjustment processes are portrayed as either caused by corrupt African regimes or as by-products of the meddling perpetrated by the imperialist US government. The one-sided accounts can at least partially be explained by the sheer complexity of the question. The economic relations that connect a Zambian subsistence farmer to the corridors of power in Washington are indeed complicated. In order to make sense of this multifaceted research question it was paramount for me, from the very beginning, to divide the question into smaller fragments.

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<sup>6</sup> The term was coined by the English economist John Williamson. Later it took on a broader meaning describing the neoliberal agenda in the developing countries more generally.

Thus, the central goal of this research can be summarized in two chronologically tied questions:

1. How did conditionality develop in the IFIs and what was the role of US influence and neoliberalism in this process?
2. How was this reflected in the case of Zambia?

In this study I will examine relationships shaped by power and authority. For this reason, I feel that it is important to point out my own position, which could be roughly located in a postcolonial terrain. My theoretical framework follows a line of thought, which its creator, Julian Go, has tentatively named “postcolonial relationalism”. Go argues that postcolonial theory and the social sciences are incompatible because of the “analytical bifurcation” inherent in the latter, meaning the pervasive practise to make a distinction between “us” and “them”.<sup>7</sup>

Go proposes a relational approach as a solution to the dilemma. Relationalism is an age-old sociological method, which emphasises the role of interactions and relations as the constitutive elements of social reality, in opposition to treating essences and substances as the static agents of existence, as is the case in relationalism’s theoretical antonym, “substantialism”.<sup>8</sup> A somewhat similar reasoning can be identified behind “connected histories”, a concept elucidated finely in the work of Gurminder K. Bhambra.<sup>9</sup> The idea of connected histories acknowledges the existence of different histories and highlights the importance of their interplay in constructing narratives that are more complete.<sup>10</sup>

However, I want to highlight the fact that my intention is not to apply this theory extensively in the study. I have chosen to include it in the introduction, because I feel that it captures my own approach in such a satisfactory way. After all, the aim of this study is not to build a comprehensive postcolonial critique of the IFI’s policies in Africa, while that in itself certainly would be a task worth considering. My goal is simply to offer a nuanced analysis by using Zambia as a case study. As a result of the relational approach, the disposition of this study may seem contrived at times, but the clear-cut separation of

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<sup>7</sup> Go 2016, 104–105.

<sup>8</sup> Go 2016, 118.

<sup>9</sup> Bhambra, 2007. The economic historian Sanjay Subrahmanyam originally formulated the idea of “Connected histories”.

<sup>10</sup> Bhambra, 2007, 33.

the questions into two distinct chapters has been essential for me in the attempt to grasp the complex subject.

In the second chapter I will delve into the evolution of the IFIs. First, I will investigate the emergence of conditional loans and track their development to becoming valid and trusted policy options in the institutions. Later, the focus will switch into tracing the influence of US authority and neoliberalism in the SAPs of the 1980s. In order to obtain comprehensive answers to these questions, an understanding of the organisational structure and voting mechanism of the IFIs is required. I will also scrutinise the similarities and differences between the Bank's and the Fund's lending policies. The second part of the chapter will focus on the years of Reagan's presidency because that era marked the expansion of SAPs in terms of both sheer number and degree of conditionality.

The IFIs are both highly complex international organisations. In studying them, I have borrowed the theoretical approach of Sarah Babb. In her own words it is best described as "broadly inspired by the institutionalist tradition within the sociology of organisations"<sup>11</sup>. This perspective highlights that, like private corporations, the IFIs are principally organisations which are dependent on their shareholders in securing their resources.<sup>12</sup> In this case, the US is by far the most important shareholder and considerable power is also wielded by other big industrial nations, namely the UK, France, Germany and Japan. Whilst this survivalist explanation describes the internal logic of the institutions, external influence is exerted in a different way. Babb argues that the organisations policies are shaped by two social systems that she identifies as national politics and expert knowledge. The end result is "policy programs"<sup>13</sup> that combine political interests and academic ideas about economics.

In the third chapter I will present the case of Zambia as a chronological account. The Zambian experience demonstrates how a relatively small and open economy, affected by global price fluctuations of a single raw material, can struggle economically and lose its economic autonomy to some degree. Given that the economic impacts of the SAPs in Zambia have been quite extensively studied, my intention is not to focus on the outcomes

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<sup>11</sup> Babb 2009, 33.

<sup>12</sup> Babb 2009, 33.

<sup>13</sup> The term was originally coined by the political sociologist John Campbell.



of the policies per se. The key question asked in the third chapter is: how did the evolution of conditionality in the IFIs and the American influence – recorded in the previous chapter – reflect itself in the case of Zambia?

In the third chapter I will mainly apply standard economic theory. In the beginning of the chapter some useful economic concepts, namely the “Dutch disease” and the so called “resource curse”, will be introduced. Despite their shortcomings, I believe the concepts to be good tools in understanding the distinct characteristics of the Zambian economy. The Zambian case dictates the temporal reach of the study as the investigation begins with Northern Rhodesia gaining independence in 1964 and ends in Kaunda losing the free elections of October 1991.

My motivation for this study stems from a couple of convictions. First, I believe that the larger public is generally unaware of the true power of the IFIs. In Finland, political interest towards the IFIs has been marginal and the relationship between the state and the institutions has been mostly sustained by civil servants.<sup>14</sup> Furthermore, the operations of the IFIs should be scrutinised thoroughly, because, more often than not, countries encountering financial crises have very little room for choice in terms of options. Most importantly, the policies formulated by the IFIs have had an effect on the lives of hundreds of millions of people.

### **1.3 Sources and Literature**

The best part in conducting a study that treats recent history is the large number of sources available. My main set of sources consists of documents of the Fund and the Bank. These papers are openly accessible in the online archives of the institutions. There is, however, a substantial difference in the openness of these organisations. While the Bank provides open access to all its documents, the Fund has historically been a lot more secretive and only opened its executive board documents for the public in 2007. In addition to historical archives, both institutions have impressive online data banks, which are open to the public. The IMF Data Mapper and World Bank Open Data centres have been extremely useful in providing some essential figures of the Zambian economy.

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<sup>14</sup> Ylönen, 2012, 8.

The Bank celebrated its first 50 years by collecting an impressive database of oral history from its former and current employees. These documents have been transcribed and they are located in the Bank's online archives. Due to the utility of the interviews I have deployed them more in the second chapter, and consequently my sources are somewhat biased toward the Bank. This partiality can be justified for two reasons. Firstly, the Bank and the Fund are in many ways very similar institutions. Their organisational structures are alike and they are both based in Washington. Secondly, most scholars would agree that the Fund has historically been more vulnerable to American influence. Thus, analogous examples of US meddling in the Bank most likely hold true with the Fund as well. The bias disappears in the third chapter as I actually utilise Fund documents more, mainly because the organisation had a slightly more decisive role in the Zambian debt crisis.

Finding secondary sources has proven rather problematic. This is not due to a lack of literature, quite the opposite. The sheer number of studies was at first somewhat overwhelming, but I have managed to find relevant books and articles amongst them. Sarah Babb presents a thorough account of the birth of the Washington Consensus in her book *Behind the Development Banks: Washington Politics, World Poverty, and the Wealth of Nations*. Likewise, Matti Ylönen's research on the history of the IFIs has provided me with some excellent insights.<sup>15</sup> The critical collection of articles edited by Jan-Bart Gewald, Marja Hinfelaar and Giacomo Macola has offered me an astute overview of the rather contested interpretations of Zambia's postcolonial history.<sup>16</sup> Another extremely useful volume in the Zambian context has been *Zambia, Mining, and Neoliberalism: Boom and Bust on the Globalized Copperbelt*, edited by Alistair Fraser and Miles Larmer.<sup>17</sup>

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<sup>15</sup> Ylönen 2012.

<sup>16</sup> Gewald, Hinfelaar & Macola 2008.

<sup>17</sup> Fraser 2010.

## 2. US Influence and the Transformation of the IFIs

### 2.1 The Early Years

In this chapter I will depict the evolution of the international financial institutions and their lending policies. I will devote a significant proportion of this chapter to the development of conditionality that led to the birth of structural adjustment programs (SAPs). Another key aspect is studying the relationship between the United States (US) administration and the international financial institutions (IFIs). My aim is to elucidate the channels of formal and informal influence between the US government and the institutions. I will also examine the somewhat turbulent relationship between the International Monetary Fund and the World Bank. A portion of the chapter will be dedicated to the battle and spread of different economic ideas and their contribution in the evolution of the IFIs. Finally, the chapter will assess the co-operation between the IFIs and Ronald Reagan's administration, which culminated in the birth of the Washington Consensus.

The IFIs were conceived in Bretton Woods as the decisive battles of the Second World War were still being waged. The leaders of the West considered the economic hardships of the inter-war years as instrumental in lifting totalitarian governments to power in Europe. Thus, international economic stability was to be a top priority after the war. The negotiations were not easy as the British and US delegations had major disagreements on central issues. To the dismay of John Maynard Keynes, the renowned economist and leader of the British delegation, the Americans were able to push their positions better. Dollars tied to gold became the customary currency in international exchanges and Washington was eventually chosen as the headquarters for both institutions.<sup>18</sup>

The Fund was designed to maintain financial equilibrium in the short time frame. Besides managing currency exchange rates, its purpose was to offer short-term capital in the form of emergency loans to nations facing severe balance of payments problems. The Bank's focus was initially on a longer time horizon. It was designed to facilitate the reconstruction of Europe after the devastating war. From the 1950s onwards, the Bank

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<sup>18</sup> Ylönen 2012, 17–21.

shifted its focus to developing countries, many of which were in the process of decolonisation. In these years the Bank was involved in project lending, mostly financing the building of infrastructure.<sup>19</sup> Almost all sovereign states of the world are members of the IFIs.<sup>20</sup>

The financing of the Fund is organised in a relatively straightforward way. Corresponding to the amount of funds that they distribute to the institution, each member state is in turn entitled to a certain quota of capital, which can be drawn in case of need. If necessary, the Fund can muster additional resources by borrowing from its members.<sup>21</sup> One of the US successes at Bretton Woods was the rejection of “automaticity”. Many other nations – including the United Kingdom (UK) – were advocating for an automatic access by members wanting to draw capital from their quotas. Instead, the US stance of “conditional” rights was written into the Articles of Agreement.<sup>22</sup> The most powerful member nation wanted to be certain that the use of Fund resources was “consistent with the purposes of the Fund”<sup>23</sup>. Although these provisions were written in a rather vague manner, Erica R. Gould maintains that they enabled the later evolution of conditional loans.<sup>24</sup>

Conditionality emerged very early as a tool in the Fund. The first conditional loans were issued in 1952 and the initiative was made by the US.<sup>25</sup> In the early years the Fund was relatively inactive as the Americans were reluctant to grant Fund loans to the European nations already benefitting from the Marshall Plan.<sup>26</sup> The original idea of the Fund had

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<sup>19</sup> Ylönen 2012, 21–24. The Bank was often involved in the technical design of projects. It usually provided about a half of the credit for the project, with the rest coming from other international donors, private lenders and local governments.

<sup>20</sup> The Fund and the Bank were officially established on 27 December 1945 and 29 nations had ratified the Articles of Agreement of the institutions by the end of the year. Under the Bank’s Articles of Agreement a country has to join the Fund first in order to secure membership in the Bank. The notable absentee from the original member nations was the Soviet Union. The Russian Federation joined both institutions in 1992. Poland withdrew from the institutions in 1950 and Czechoslovakia was expelled four years later. The countries were readmitted in 1986 and 1990 respectively. Cuba left in 1964 and has not joined since. Today the Bank and the Fund both have 189 member nations. In addition to Cuba there are four countries in the United Nations (UN) that are not members: Andorra, Liechtenstein, Monaco and North Korea. Zambia joined the Fund and the Bank in 1965 shortly after gaining independence. (IMF website, 6 March 2018. *List of Members*; World Bank website, 6 March 2018. *Member countries*.)

<sup>21</sup> IMF website, 6 March 2018. *Where the IMF Gets Its Money*.

<sup>22</sup> Gould 2006, 41.

<sup>23</sup> Gould 2006, 41. Quoted from the Bretton Woods agreement.

<sup>24</sup> Gould 2006, 42.

<sup>25</sup> Gould 2006, 40.

<sup>26</sup> The Journal of Commerce, 6 March 1952. The Marshall Plan was an American scheme that was designed to assist in the reconstruction of Western European states. The total amount of aid reached 13 billion US dollars, equating approximately 140 billion dollars today.

been to assist the more developed countries in urgent need of help, but soon it was granting loans mainly to developing nations.<sup>27</sup> It is evident that the Americans wanted stronger conditionality partly because of this shift in attention. Compared to later meticulous standards, the early conditions were more moderate and tied to “broad macroeconomic targets”<sup>28</sup>. Their aim was to stabilise balance of payments in order to combat devaluation of currencies and inflation. In my opinion, the adoption of these loan policies is a clear sign of the early US hegemony in the Fund. This US dominance is implied in a piece from The Journal of Commerce treating the changes in lending policy back in March 1952:

”It reflects some easing of the stringent U.S. position and is designed to encourage members to seek modest assistance from the Fund. At the same time, it has been written in such a way as to make it crystal clear that there is to be no “automatic access” and that the Fund will continue to apply rigorous standards to every request.”<sup>29</sup>

The first conditional loans were named Stand-by Arrangements (SBAs). The SBA was designed not to be a “loan per se but rather an assurance of automaticity: that the Fund will loan within a certain period of time under certain conditions”<sup>30</sup>. In the following decades the conditional loans changed radically: the number of binding conditions grew and the nature of the conditions altered considerably “reflecting a shift toward ‘microconditionality’”<sup>31</sup>.

The International Bank of Reconstruction and Development (IBRD)<sup>32</sup>, as the Bank was known in its early years, was also struggling to find its feet in the post-war years. In 1949, when the remarkable reconstruction of Europe was well under way, an American banker, Eugene Black, was chosen as the president of the Bank (1949-1961). Under his guidance the Bank hired a vast number of economists and concentrated its efforts on project lending

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<sup>27</sup> Ylönen 2012, 21.

<sup>28</sup> Gould 2006, 40.

<sup>29</sup> The Journal of Commerce, 6 March 1952.

<sup>30</sup> Gould 2006, 48.

<sup>31</sup> Gould 2006, 59, 67.

<sup>32</sup> IBRD is still one of the organisations that comprise the World Bank Group. The other main agencies are the International Finance Corporation (IFC, founded in 1956), the International Development Association (IDA, 1960), the International Centre for Settlement of Investment Disputes (ICSID, 1965) and the Multilateral Investment Guarantee Agency (MIGA, 1988). In addition, it is also important to note that the World Bank is not the only big multilateral development bank in the world. It has four main regional competitors: The Inter-American Development Bank (IDB, 1959), the Asian Development Bank (AsDB, 1965), the African Development Bank (AfDB, 1964) and the European Bank for Reconstruction and Development (EBRD, 1991).

in developing countries.<sup>33</sup> Single conditions were sometimes attached to loans, but describing the policies as conditional lending would be an overstatement. For example, in order to receive a loan for a power plant, the Bank could demand the borrowing state to push up its tariffs on electricity so that the plant would be profitable.<sup>34</sup>

The Bank's three main sources for obtaining its operating resources are member contributions, the interest from bonds that the Bank issues on global financial markets and loan reflows, which means repayments of principle with interest added on.<sup>35</sup> Although the Bank's budget increased in the 1950s and the early 1960s, the lending amounts at that time were considered by a later employee as "comparatively small"<sup>36</sup>. Furthermore, the Bank was not enjoying a very high status in the international financial market. Before his tenure in the Bank, the same employee was working for the US administration and according to him "everybody in the US government regarded the World Bank and the International Financial Corporation (IFC), which it had established in the late '50s, really as a joke, long on public relations, but short on performance"<sup>37</sup>. This contemptuous attitude would change in later years.

A turning point in the Bank's lending policies was seen in 1960 when the International Development Association (IDA) was established. Four years earlier the Bank had created the International Financial Corporation (IFC). The IFC was designed to encourage private business by channelling loans straight to firms. By contrast, the IDA is catered to serve the needs of low-income countries. The IDA's "soft loans" are repayable in 50 years and, most importantly, they bear no interest. Unlike most of the Bank's other lending facilities, the IDA is heavily dependent on contributions from its member states. This gives considerable power to the wealthier nations. The US share of the first "replenishment"<sup>38</sup> was 42 percent.<sup>39</sup>

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<sup>33</sup> Ylönen 2012, 27.

<sup>34</sup> Ylönen 2012, 56.

<sup>35</sup> Babb 2009, 24.

<sup>36</sup> Interview with Bernard R. Bell, 13 November 1985 and 28 January 1988: First session, 19. World Bank Group, Oral History Program.

<sup>37</sup> Interview with Bernard R. Bell, 13 November 1985 and 28 January 1988: First session, 19. World Bank Group, Oral History Program.

<sup>38</sup> The IDA raises its funds every three years. The 18<sup>th</sup> successive replenishment was finalised in December 2016. (World Bank website, 7 March 2018. *IDA: Replenishments*.)

<sup>39</sup> Ascher 1990, 117–118.

The American role in the launching of the IDA was crucial. By the end of the 1950s, the number of sovereign states in the world was rising at a significant pace. The newly independent countries were able to acquire considerable power in the United Nations due to the general assembly's one-country one-vote system.<sup>40</sup> Development in the so-called "Third World" thus became a hot topic in the UN, and in 1953 its Economic and Social Council came up with a detailed plan for a new agency, SUNFED (the Special United Nations Fund for Economic Development). Similarly to the later IDA, the purpose of SUNFED was to offer concessional loans and grants to developing countries.<sup>41</sup> Not surprisingly, the US government took a critical stance towards SUNFED. The Bank's former Vice-President J. Burke Knapp recalls the strong US input in establishing the IDA:

"The issue, therefore, between SUNFED and IDA became rather acute at one time, and it was the United States government primarily that decided to go for an agency under the management of the World Bank rather than one under the management of the United Nations. The considerations were twofold: one, that an agency administered under the United Nations would presumably be dominated by the underdeveloped countries if the voting was on a unit basis, complicated by the fact that in the United Nations the Soviet Union and the rest of the iron curtain countries would be members and participate in the management. And for those rather obvious political reasons, the United States felt that it would rather contribute its money to something under sounder professional and technical management than could be expected under the United Nations administration."<sup>42</sup>

Notwithstanding the rather smug attitude that Knapp holds for the Bank's management, compared to corresponding management by the UN, his conclusions about US reasoning in this case are probably correct. Noting the strong antagonism toward communism, Babb agrees that the US opposition to SUNDFED "seems to have resulted from a combination of ideological and geopolitical factors"<sup>43</sup>. For the purpose of this study, however, the bottom line that can be drawn from this and earlier observations is the following deduction: in the early years of their existence the IFIs were quite firmly in US control. American persistence led to the adoption of conditionality in the Fund and the birth of the IDA testifies that the Americans were also able to guide the Bank toward a path of their preference.

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<sup>40</sup> Babb 2009, 22.

<sup>41</sup> Ylönen 2012, 24.

<sup>42</sup> Interview with J. Bruce Knapp, July 1961, 36. World Bank Group, Oral History Program.

<sup>43</sup> Babb 2009, 22.

## 2.2 Channels of Influence

Tracing US influence in the early years is not difficult since the IFIs (especially the Fund) were generally regarded as institutions led by the interests of the American government.<sup>44</sup> However, it is important to analyse how this authority was precisely exerted, because the channels of influence remained essentially the same later when the IFIs gained more autonomy. Ngaire Woods provides us with a useful four-point division of different channels of influence. The four channels of influence include: formal structures of voting and power; financial structure; use of resources; staffing and management.<sup>45</sup> Because of its clarity, I will implement the same categorisation here.

The first channel is the most official one as it embodies the formal decision making of the IFIs. The organisational structures of the Bank and the Fund are very similar. Both institutions have a board of governors which meets once a year to discuss overall strategy, while formal decisions are made in the executive board.<sup>46</sup> Directors in the executive board represent all member states, but rich countries are favoured because voting quotas are divided in a complex procedure that emphasises the size of the economy. Thus, for example, Bangladesh, with a population roughly half the size of the US, has 12 131 votes in the Fund, while the American director wields 831 407 votes equalling a total of 16.5 percent.<sup>47</sup> In the Fund, all major decisions and changes in the voting structure require an 85 per cent majority meaning that the US has an effective veto.<sup>48</sup> In the Bank, the US holds a similar veto and it has proven determined to hold on to it. In a telling example from 1988, the US Congress discussed granting new funds to the Bank in conjunction with a reshuffle of the voting shares which would see the US portion drop to 18.75 percent. Under pressure from Congress, the Bank complied to alter the constitutional majority from 80 to 85 percent consequently securing the US veto.<sup>49</sup>

The second channel of influence is tied to the financing of the IFIs. As can be expected, in addition to holding most votes, the US is also the most important financial donor. However, a substantial part of US power does not derive directly from its large contributions. The extra authority originates from the unique political system in the US.

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<sup>44</sup> Woods 2003, 92; Kahler 1990, 92.

<sup>45</sup> Woods 2003, 96–97.

<sup>46</sup> Woods 2003, 110.

<sup>47</sup> IMF website, 6 March 2018. *IMF Members' Quotas and Voting Power, and IMF Board of Governors*.

<sup>48</sup> Ylönen 2012, 200.

<sup>49</sup> Babb 2009, 137.



Because executive and legislative powers are so clearly separated, Congress can have substantial disagreements with the president's cabinet. Consequently, congressional opposition has made the formulation of consistent foreign aid policies hard for the government.<sup>50</sup> The regular increases to Fund quotas and replenishments of the IDA require the approval of Congress. While leading to internal disputes between Congress and the administration, it can be argued that the power of the former can work as a handy tool for the latter as well. With the continuous threat of diminishing funds, the US government has been able to push its policies in the IFIs.<sup>51</sup>

Babb labels this US activist shareholder position as having “donor leverage”. According to her, it is probably the “most important mechanism” of US influence and regularly used when donor governments meet to discuss funding: “in these negotiations, the United States is notorious for being the squeaky wheel – the shareholder with the most demands and complaints and the one least willing to compromise”<sup>52</sup>. The US treasury has a monopoly in formulating policies directed at the Fund, but its authority is boosted markedly by the fact that additional contributions to the institution must be approved by Congress.<sup>53</sup> Relations to the Bank are upheld mostly by the State Department. Although the Bank is more independent in its funding, donor leverage becomes visible every time a new IDA replenishment is discussed, and this has provided an additional channel of influence for the US government.

Because the US is the most important shareholder, its congressional battles are often followed closely by other industrial countries. Thus, the US holds a key position because other donors tend to follow its lead. Ernest Stern, whose career at the Bank spanned 27 years, describes how important it was to first secure US commitment:

“But the US, as the single largest contributor, defined the range of possible conclusions. No other donor was prepared to compensate for a further decline in the US share. And the problem was compounded by the fact that the US had by far the most extensive policy demands. So they generally managed to set everybody's teeth on the edge early in all the discussions.”<sup>54</sup>

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<sup>50</sup> Babb 2009, 14.

<sup>51</sup> Woods 2003, 99–100.

<sup>52</sup> Babb 2009, 13.

<sup>53</sup> Woods, 2003, 99.

<sup>54</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Fourth session, 41–42. World Bank Group, Oral History Program.

This extract reveals in an unequivocal way the strength of US influence and, furthermore, the willingness of the Americans to promote their own aspirations in the institutions. According to Stern “there was always, particularly on the U.S. side, a strong drive for imposing policy conditions”<sup>55</sup>. The strong push for US objectives can be seen when the capital of the Bank was increased in 1988, as discussed earlier. In addition to the change of the constitutional majority – which secured the US veto – the Americans were able to ensure that the Bank was committed to “increased efforts to help design and implement adjustment programs and to assemble debt restructuring packages”<sup>56</sup>. There is no reason to believe that the Americans operated any differently with the Fund.

The third outlet of influence involves the use of the IFI’s resources. US interference becomes visible in the cases where the Americans have opposed loans for political reasons. A commonly cited example is the US led interruption of the Bank’s lending operations in Chile during the reign of Salvador Allende’s left-wing government (1970–1973).<sup>57</sup> However, cases giving rise to public objection are relatively rare, since the US is able to pressure the IFIs before the loans are talked over in the executive boards of the institutions. Burke Knapp sums this mechanism up in a neat way:

“However, at the same time there are occasions in which it’s useful to take a reading on what is current United States policy in some countries in which we’re operating. We are very sensitive about this. We strongly maintain our autonomy and independence, to the point where many State Department officials and many American ambassadors abroad are rather resentful of our stiff-necked attitude. But we do feel that it would be very damaging to us to be regarded as a political instrument of the United States. On the other hand, United States is our principal shareholder. They provide a large part of the money required by the Bank and its operations, and de facto the United States government could always mobilize a majority of the board against any project on which they wanted to impose a political veto. I should emphasize that this happens on only very rare occasions. But if there is any doubt as to whether the United States government will support an operation by the Bank, it’s just as well for us to know that at an early state of the game, and the way we usually find that out is through contacts with the State Department.”<sup>58</sup>

Understandably, Knapp fervently defends the autonomy of the Bank. Nonetheless, the lengthy quotation uncovers the extensive reach of US influence. While Knapp underlines the sporadic nature of US interventions, it is important to note that his interview dates

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<sup>55</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Fourth session, 39. World Bank Group, Oral History Program.

<sup>56</sup> Babb 2009, 137. Quoted from the US Congress House Appropriations Subcommittee, Appropriations for 1989, 1043.

<sup>57</sup> Ascher 1990, 124; Babb 2009, 40.

<sup>58</sup> Interview with J. Bruce Knapp, July 1961, 40. World Bank Group, Oral History Program.

back to 1961. Although the Cold War was “freezing” at the time, the struggle between the Western and Eastern blocs over the political alignment of the developing countries would only intensify in the following years. Thus, by the 1970s, US relationship with the IFIs had become more strained and interventions more common.<sup>59</sup> A former legal expert in the Bank, Aron Broches, is more straightforward in admitting that the US did get “special treatment”.<sup>60</sup> According to Broches it was an accepted custom that “loan proposals, or the documents before they went to the Board, were shown to the U.S.”<sup>61</sup>. Lastly, one cannot stress enough the fact that the IFIs are based in the US capital. This physical proximity in Washington has surely facilitated the special relationship between the US government and the IFIs.

The fourth channel of influence is very indirect and, for that reason, the hardest one to detect. Historically, Americans have been overrepresented in the staffs of the IFIs. The Americans lobbied successfully against national quotas for personnel (which for example the UN has) and promoted English as the working language.<sup>62</sup> In the early years of the institutions one could almost speak of US hegemony, although the proportion of Americans has declined significantly since. In the Bank, 64 percent of the professional staff were Americans in 1950, but by 1968 their share had dropped to 31 percent and in 1987 to 24 percent.<sup>63</sup> A similar trajectory, an early American dominance followed by a decline, holds true for the Fund as well.<sup>64</sup> The American presence is especially true in the higher levels of management. The managing director<sup>65</sup> of the Fund is traditionally of European origin. However, the Americans have considerable power in choosing the person for the position.<sup>66</sup> In addition, the deputy managing director, with close ties to the US treasury, has always been American.<sup>67</sup> In the Bank, the Americans have the power to

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<sup>59</sup> Babb 2009, 61–62.

<sup>60</sup> Interview with Aron Broches, 18 April and 23 May 1984: First session, 14. World Bank Group, Oral History Program.

<sup>61</sup> Interview with Aron Broches, 18 April and 23 May 1984: First session, 14. World Bank Group, Oral History Program.

<sup>62</sup> Woods 2003, 108.

<sup>63</sup> Ascher 1990, 125.

<sup>64</sup> Kahler 1990, 97.

<sup>65</sup> The managing director of the Fund is the leader of staff and chairman of the executive board. The president holds an analogous position in the Bank.

<sup>66</sup> Kahler 1990, 94.

<sup>67</sup> Woods 2003, 109; Kahler 1990, 94.

appoint the president who has always been a citizen of the US.<sup>68</sup> This brings a sense of ambiguity to this position, which can be read in the comments of former President Black:

”The President of the Bank is an international character, and his liaison with the US government is through the American Director. As a matter of fact, the President of the Bank, if he stays in Washington very long, gets to know the officials, and quite frequently has meetings with them, but that’s not the normal procedure. Of course, in my case I happened to be an American. I knew all these people personally, and quite frequently had talks with them.”<sup>69</sup>

Black emphasises that relations between the president of the Bank and the US government should be conducted through the official way (the American director). Nevertheless, direct meetings between the US government officials and the president of the Bank are common. This implies that there is a possible channel of US influence embedded in the informal networks linking the IFIs to the White House and Capitol Hill. However, in my opinion, it is impossible to draw conclusive evidence of US influence by using the number of Americans in the technical staff and management of the IFIs as a yardstick. After all, the institutions are multilateral and committed to work for the common good. Strong American presence in the IFIs does enable a channel for US influence but by no means does it necessitate the use of it. The picture becomes more complex in later years. While the ethnic diversity in the IFIs expanded, an overwhelming majority of the staff’s economists have graduated from Anglo-Saxon universities.<sup>70</sup> There is a strong case in assuming that this facilitated the spread of certain economic ideas. I will turn to this question later.

The formal structure of voting was seen as an important channel of US influence in the early years of the institutions.<sup>71</sup> It is safe to assume that this channel lost its early prominence as time passed and more unofficial links were forged between the IFIs and the US administration. In fact, I agree with Babb in her assessment that the formal structure of voting is not the most important channel of influence.<sup>72</sup> Most likely the fourth channel is also not that central, and I would argue that, while this channel is important in spreading economic ideas, its significance as a direct channel of US influence should be doubted.

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<sup>68</sup> Babb 2009, 40.

<sup>69</sup> Interview with Eugene R. Black, 6 August 1961, 25. World Bank Group, Oral History Program.

<sup>70</sup> Woods 2003, 109.

<sup>71</sup> Kahler 1990, 96.

<sup>72</sup> Babb 2009, 66.

It is the second and third channels of influence that we must turn to. In my opinion both are vital because they are used to achieve slightly different goals. The US government is able to pressure the allocation of IFI resources by using the informal networks linking the headquarters of the institutions to Capitol Hill and to the White House in Washington. Only rarely is the US government publicly forced to confront the IFIs when it disagrees about the use of resources. In comparison, donor leverage – derived through congressional opposition – is not used to achieve quick political outcomes. The purpose of this channel of influence is to guide the institutions toward a favoured course in the longer time frame.

## **2.3 Crises Fuel Conditionality**

From their very conception the IFIs have been adapting to changes in their operational environment. By the 1970s the international monetary regime was under increasing pressure. The liquidity of the Bretton Woods system was strained as the Vietnam War accelerated the outflow of dollars from the US and resulted in the overvaluation of the currency. Simultaneously, Japan and the European block emerged as serious economic rivals to the Americans and the US role of “international treasury keeper” was questioned. The governmental control over the financial milieu became more challenging as the free movement of private capital was gradually relaxed.<sup>73</sup> In 1971, President Richard Nixon (1969–1974) announced that the US would end the dollar’s convertibility to gold and let the currency float. The effects of the “Nixon shock” were further compounded by the first oil crisis<sup>74</sup> in 1973 and other commodity price jolts.

The collapse of the Bretton Woods system came at an especially critical moment for the Fund. The institution was customised for the needs of the system. The Fund had been created to oversee fixed currency exchange rates which were now allowed to float freely. Ylönen notes how the end of the Bretton Woods system practically destroyed the

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<sup>73</sup> Blyth 2002, 128–129.

<sup>74</sup> The oil crisis erupted in October 1973 when the Organisation of Arab Petroleum Exporting Countries (OAPEC) declared an embargo. The oil producing nations were experiencing declining earnings because of the weakness of the dollar. As a result of the embargo, the price of an oil barrel quadrupled from approximately three dollars to twelve dollars. Although the embargo was targeted at certain Western industrial nations, that were supporting Israel in the Yom Kippur War, it had long-lasting consequences for the entire global economy. The second oil crisis began in 1979 following the Iranian Revolution. Decreases in oil output and a panic in the market more than doubled the price of oil in a year.

operating mandate of the Fund and forced it to alter the rationale of its operations. The Fund took on new responsibilities by expanding its lending in struggling developing countries and this paved the way for SAPs.<sup>75</sup> Combating inflation had been one of the core aims of the Fund from the very beginning and from this perspective the 1970s brought increasing challenges.<sup>76</sup> From the end of the 1960s the stagnation of the world economy was accompanied with increased inflationary pressures.<sup>77</sup> Conditionality developed to a useful instrument for the Fund in this battle.

The Fund's conditional loans had developed considerably in twenty years. The number of binding conditions grew steadily and new forms of conditional loans were introduced.<sup>78</sup> The Fund created the Compensatory Financing Facility (CFF) in 1963. This was followed by the Oil Facility (1974), Extended Fund Facility (EFF, 1974) and the Trust Fund (1976).<sup>79</sup> For the purpose of this study it is not necessary to delve too deeply into various technical aspects of the different loan facilities. However, it is important to note that the establishment of the last three loan windows was surely motivated by the collapse of the Bretton Woods system. In a sense, the Fund had to recreate itself and the new innovations were designed to assist it in this metamorphosis.

Thus, it was no surprise that increased conditionality became a topic of passionate debate. In June 1978 the issue was discussed extensively in the executive board meeting of the Fund. Conditionality had already developed so far that abandoning it altogether was not

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<sup>75</sup> Ylönen 2012, 23.

<sup>76</sup> The Fund's economic policies are grounded on the assumption that low inflation fosters economic growth. The recipe for tackling high inflation is based on a couple of principles and these are typically seen in the conditional loans issued by the institution. Central banks are asked to push interest rates up, the eradication of price controls requested and fiscal austerity demanded. While the Fund's methods in combating inflation are rarely questioned, the general logic of minimising inflation has been hotly debated. All scholars surely agree that excessive inflation is harmful to an economy but the level of sustainable inflation is disputable to say the least. The Fund has been criticised because of its insistence on very low inflation rates. (Ylönen, 2009, 85–92.)

<sup>77</sup> The economic circumstance of rising inflation and slackening economic growth, described above, is known as “stagflation”.

<sup>78</sup> Gould 2006, 59–60.

<sup>79</sup> The Compensatory Financing Facility was designed to help countries that were producing primary products and facing falls in exports. The CFF-loans were relatively low-conditional. The Oil Facility was created in the aftermath of the first oil crisis. Its purpose was to aid economies that were hit hard by the rising oil prices. The first Oil Facility in 1974 offered loans with only a few conditions. The second Oil Facility (open from January 1975 to May 1976) was more conditional as borrowers were required to accept a Fund policy program. The Extended Fund Facility was the clearest step to a new direction as it differed from the old SBA in an important way. The EFF loans were also high in conditionality but designed to help with problems in the medium term. Instead of fixing desperate balance of payment problems, this meant adjusting structural problems of the economy and tackling persistent low growth. Finally, the Trust Fund's aim was to offer loans on concessional terms to “eligible developing countries”. (Gould 2006, 60–62.)

seen as an option. According to one of the executive directors at the time, Muhammad Al-Atrash, “the issue at present is not whether there should or should not be conditionality. There is no disagreement that conditionality is necessary. But the issue is how much conditionality”<sup>80</sup>. Al-Atrash propagated for less conditionality claiming that “many countries feel that if they have to seek Fund assistance in the higher credit tranches, they have practically to nearly surrender their sovereignty in the economic field”<sup>81</sup>. Others shared his view as more “clear-cut and limited objectives for conditionality”<sup>82</sup> were demanded. These appeals were not heard as the executive board’s guidelines for conditionality, approved in March 1979, testify. The fourth paragraph of the guidelines states:

“In helping the members to devise adjustment programs, The Fund will pay due regard to the domestic social and political objectives, the economic priorities, and the circumstances of members, including the causes of their balance of payments problems.”<sup>83</sup>

In addition to this vague passage the ninth paragraph affirms that “performance criteria will normally be confined to (i) macroeconomic variables (ii) those necessary to implement specific provisions of the Articles or policies adopted under them”<sup>84</sup>. Performance criteria refers here to specific conditions. Although these can be viewed as relatively precise guidelines, one cannot but wonder how to interpret the wording “normally” in this case. In this light, the guidelines are reminiscent of the indefinite provisions which the Americans were able to include in the Articles of Agreement at Bretton Woods.

Some conclusions can be drawn here. Firstly, it is evident that – quite understandably – the directors who opposed strong conditionality represented developing countries. Their calls for regulated conditions did not materialise in the final edition of the guidelines and this reflects the power imbalance toward developed countries and especially the US. While several directors were heard in earlier meetings, the American director, Sam Y. Cross, wrote his statement conveniently a day before the executive board meeting in

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<sup>80</sup> Statement by Mr. Al-Atrash on Conditionality - EBM/78/80 (6/2/78), 2. BUFF/78/64, 6/5/1978. IMF Archives.

<sup>81</sup> Statement by Mr. Al-Atrash on Conditionality - EBM/78/80 (6/2/78), 2. BUFF/78/64, 6/5/1978. IMF Archives.

<sup>82</sup> Statement by Mr. Mayobre on Conditionality - EBM/78/79 (6/2/78), 1. BUFF/78/59, 6/1/1978. IMF Archives.

<sup>83</sup> Guidelines on Conditionality, 1. SM/78/296, Rev. 1, Sup. 3, 3/5/1979. IMF Archives.

<sup>84</sup> Guidelines on Conditionality, 2. SM/78/296, Rev. 1, Sup. 3, 3/5/1979. IMF Archives.

which the guidelines were ratified in March 1979. Cross endorsed the proposed guidelines and viewed the two provisions – discussed above – as “important safeguards”<sup>85</sup>. In my opinion, the timing of Cross’s statement indicates implicitly the decisive role of the US in formulating the Fund’s policies. The second deduction stems from the theoretical framework of studying organisations from a sociological perspective. From this point of view it would have made no sense for the Fund to draw strict guidelines that would tie the organisation down. The internally led transformation of Fund policies had largely been enabled by the vague formulations in the original Articles of Agreement.

After defeating the internal opposition the Fund had to justify its new approach to the outside world. That is exactly what the Fund’s Director of Western Hemisphere Department, E. Walter Robichek, set out to do in his speech delivered at the Center for Latin American Monetary Studies (CEMLA), Mexico City, in July 1979. Robichek acknowledged the criticisms levered against conditionality but proceeded to defend the Fund’s approach:

”Adjustment programs supported financially by the Fund do not lend themselves to standardization. Each program needs to be compatible with the structure of a country’s economy and with its institutional framework. Adjustment programs will, therefore, vary from country to country. Each program also needs to address the causes and the severity of a country’s payments problem, and hence even programs negotiated with the same country may well differ over time.”<sup>86</sup>

This extract presents the central argument in rejecting uniform rules for conditionality. Because each specific case is different, the Fund needs room to manoeuvre in designing correct adjustment policies. Robichek dismissed the issue of losing national sovereignty on the grounds that “giving an international institution important regulatory powers over policies and behaviour of member countries, as the Fund was given, obviously involves a sharing of national sovereignty”<sup>87</sup>. Furthermore, he blamed the press and other media of portraying the negotiations of loan programs as “confrontations between the national authorities and the Fund”<sup>88</sup>. Although Robichek was expressing his private opinions about conditionality, it is clear that he was representing the official line of the Fund, approved earlier that year.

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<sup>85</sup> Guidelines on Conditionality, 1. *EBD/79/58*, 3/1/1979. IMF Archives.

<sup>86</sup> The Conditionality of the IMF - CEMLA Seminar - Mexico City, 7. 7/30/1979. IMF Archives.

<sup>87</sup> The Conditionality of the IMF - CEMLA Seminar - Mexico City, 15. 7/30/1979. IMF Archives.

<sup>88</sup> The Conditionality of the IMF - CEMLA Seminar - Mexico City, 15. 7/30/1979. IMF Archives.



As noted before, the number of binding conditions had grown over the years but, most importantly, the nature of the conditions had changed along the way as well. Instead of addressing acute fiscal problems, the conditions were increasingly designed to confront structural problems in the economy and low rates of growth.<sup>89</sup> From the 1980s onwards Fund loans were usually accompanied with SAPs “that address chronic balance of payments shortfalls and low growth, and often entail long-term, supply-side policies, such as deregulating domestic goods, eliminating price controls, deregulating financial markets, eliminating interest rate ceilings, liberalising trade”<sup>90</sup>. The Fund reviewed its policies on conditionality in an executive board meeting in April 1988. According to the chairman’s survey the directors felt that the 1979 guidelines “had served us well” but added that the Fund “needs to place more emphasis on structural reforms and growth-oriented adjustment”<sup>91</sup>. Thus, after the revision of key functions in the 1970s, structural adjustment had taken the centre stage in the Fund’s policies by the next decade.

In the 1970s the Bank was going through a significant transformation of its own. A new era began in 1968 when Robert S. McNamara was appointed as the president of the Bank (1968–1981). The Bank had been regarded as a conservative institution but under McNamara and Vice-President Hollis Chenery development economics became the new focal point.<sup>92</sup> The Bank had taken steps into this direction under the previous president, George D. Woods (1963–1968), but his staff had consisted overwhelmingly of engineers and economists. Emphasising the change brought by McNamara, a former employee of the Bank commented on the situation before the new president was appointed, “I don’t believe we even had a sociologist at the Bank”<sup>93</sup>.

The institution moved its attention to longer-term goals and took on new initiatives like rural development, provision of social services and upgrading of urban slum areas.<sup>94</sup> Ernest Stern claims that “it wasn’t until McNamara came along that population, education, human resources, agriculture, rural development and income distribution

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<sup>89</sup> Gould 2006, 66.

<sup>90</sup> Gould 2006, 66.

<sup>91</sup> The Chairman’s Summing Up of the Discussion on Conditionality - A Survey of Current Issues - EBM/88/60 (4/8/88), 4. *BUFF/88/74*, 4/11/1988. IMF Archives.

<sup>92</sup> Babb 2009, 49.

<sup>93</sup> Interview with Michael Lejeune, 17 July and 19 November 1985: Second session, 11. World Bank Group, Oral History Program.

<sup>94</sup> Ascher 1990, 120.

emerged as development policy foci”<sup>95</sup>. The Bank started publishing its renowned World Development Report in 1978. The new agenda was epitomised in the enthusiastic and vigorous character of the president. In 1973, in a famous speech in Nairobi, McNamara declared that alleviating poverty from the world was the central aim of the Bank.<sup>96</sup> In order to pursue these ambitious objectives, the Bank had to increase its budget substantially. During McNamara’s tenure the Bank’s lending increased fivefold in real terms.<sup>97</sup> In addition, the Bank started to issue loans for state-owned industrial projects. Before the 1970s the Bank had been reluctant to extend its lending beyond the private sector.<sup>98</sup>

After an exciting start the mood had shifted in the Bank by the end of the 1970s. Despite vast investments, the long-awaited “take-off” in the developing countries had never occurred. On the contrary, in many cases their situation had deteriorated because of the energy crisis and escalating indebtedness. This realisation prompted a change in policies as project lending was increasingly supplemented or replaced with policy-oriented program loans.<sup>99</sup> Program loans differed from project loans in that they were not issued to finance certain development projects. Their aim was to help finance imports and they “were loosely connected to market-liberalising policy reforms”<sup>100</sup>. Although project loans had dominated Bank lending, it had also undertaken some program lending before the 1970s.<sup>101</sup>

By the end of the decade McNamara had singled out program lending as an avenue for promoting longer-term development in the poor parts of the world. In 1979, McNamara introduced his version of structural adjustment in an address to the United Nations Conference on Trade and Development (UNCTAD) in Manila. In the address McNamara identified trade imbalances as a key factor in preventing economic progress and urged “that the international community consider sympathetically the possibility of additional assistance to developing countries that undertake the needed structural adjustments for

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<sup>95</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Second session, 12. World Bank Group, Oral History Program.

<sup>96</sup> Ylönen 2012, 28.

<sup>97</sup> Ascher 1990, 120. The calculation is from Robert Ayres’ book *Banking on the Poor* (1983) and it discounts inflation.

<sup>98</sup> Ascher 1990, 120.

<sup>99</sup> Ascher 1990, 121.

<sup>100</sup> Babb 2009, 102.

<sup>101</sup> An internal report of the Bank estimates that prior to 1968 about 4 per cent of the Bank’s loans were program loans. (Babb 2009, 102.)

export promotion”<sup>102</sup>. Stern, a senior vice-president at the Bank who was in charge of the lending operations from 1980 to 1987, explains the rationale behind the Bank’s adoption of structural adjustment loans (SALs):

”It did arise out of the oil crisis, and its impact on the developing countries. It was the beginning of defining concerns with the structural aspects of balance of payments adjustments rather than focusing solely on the macroeconomic aspects. The concept that structural problems were at the core of the balance of payments difficulties facing many developing countries was not common then. The solution to balance of payments problems was generally believed to be macroeconomic adjustments. Our original concept was to help countries take action in advance of a deterioration in the balance of payments.”<sup>103</sup>

Stern is placing his words with care here. One of the clearest arguments in objecting to structural adjustment by the Bank is that, by doing so, one is stepping on the toes of the Fund. Stern maintains that, instead of dealing with an acute balance of payments predicament, the Bank’s structural lending is aimed at fixing the underlying problems that cause the crisis, preferably before it starts. Stern proposed his version of structural lending to the executive board in February 1980. Babb argues that Stern had deviated from McNamara’s original vision and “placed greater emphasis on policy conditionality”<sup>104</sup>. Compared to the traditional project loans, the SALs usually involve larger sums, have to be paid back sooner (three to five years usually) and “rely on macroeconomic expertise and assessments of general economic policy”<sup>105</sup>. While the Bank’s SALs differed from the Fund’s counterparts in that they were targeted at longer-term adjustments and directed to the more fundamental structural problems in an economy, the loans did have a lot in common. In Babb’s words they both “began with a quasi-contractual agreement between staff and borrowing governments concerning policy changes, including statements of measures, or “benchmarks” for gauging government compliance”<sup>106</sup>.

Stanley Please worked under Stern as the senior adviser on SALs from 1980 to 1983. According to him the initial opposition to the new loan form was severe in the executive board, and, unlike many other issues, it did not follow the usual North-South divide:

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<sup>102</sup> McNamara 1979, 29. *Address to the United Nations conference on trade and development by Robert S. McNamara, President of World Bank (English)*. Presidential speech. World Bank Archives.

<sup>103</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Third session, 21. World Bank Group, Oral History Program.

<sup>104</sup> Babb 2009, 105.

<sup>105</sup> Ascher 1990, 121.

<sup>106</sup> Babb 2009, 105.

”The developed countries felt that the Bank was moving from its mandate in supporting development into quick-disbursing non-project lending, and developing countries took the view that one IMF was enough on policy matters”.<sup>107</sup>

Despite of the hostility in the board the Bank pushed on with the SALs. The board was able to secure concessions, such as the guarantee to restrict program lending to ten per cent of the Bank’s total operations. Please notes, however, that probably the most crucial reason for adopting structural adjustment was external, as the debt crisis hit Latin America and Africa hard in the early 1980s.<sup>108</sup>

The breakdown of the Bretton Woods system and turmoil in the global economy had a profound effect on the US relationship with the IFIs. When the Fund was practically struggling for its existence, the US government turned its attention to other international bodies. Woods explains how the US government marginalised the Fund on purpose and promoted economic collaboration through the novel Group of Seven (G7)<sup>109</sup> and the older Group of Ten (G10). According to her, the rejection was a striking piece of evidence of the US power to determine the fate of the Fund.<sup>110</sup> Thus, when the Fund took a leading role in tackling the debt crisis in the next decade, it should be viewed both as a testimony of US approval but equally, as Woods highlights, as an attempt of a side-lined organisation to get back into action.<sup>111</sup> Even though the US government turned to other options in its efforts to fix the global monetary system, its influence on the Fund remained relatively strong, albeit not as dominating as before. Miles Kahler notes how the US was forced to use special majorities (70 and 85 percent in important matters) due to decreases in its voting quota. While this meant more extensive bargaining with other members, the special majorities functioned also as safeguard to US interests.<sup>112</sup>

Although conditionality evolved in the Fund through the 1970s, the environment was not yet favourable for full implementation. The main reason for this was the abundant supply

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<sup>107</sup> Interview with Stanley Please, 26 August 1986, 15. World Bank Group, Oral History Program.

<sup>108</sup> Interview with Stanley Please, 26 August 1986, 18–19. World Bank Group, Oral History Program.

<sup>109</sup> The G7 was established in March 1973 just before the oil crisis. The forum’s purpose was to draw macroeconomic guidelines for the global economy following the Nixon shock. Later it was engaged in finding solutions to the energy crisis and the subsequent recession. The group consists of Canada, France, Germany, Italy, Japan, the UK and the US. These days the European Union (EU) is also represented at the meetings. The G10 is a group of countries that decided to provide the Fund with additional funds back in 1962. In addition to the G7 countries it includes Belgium, the Netherlands and Sweden. Switzerland joined the club in 1964.

<sup>110</sup> Woods 2003, 94.

<sup>111</sup> Woods 2003, 94.

<sup>112</sup> Kahler 1990, 100.

of cheap private credit which made the Fund's conditional loans unappealing.<sup>113</sup> The removal of barriers restricting the free movement of capital began from London in the 1960s. The vast accumulation of dollars there was facilitated by the creation of the Euromarkets which did not fall under the regulations of the US or the UK.<sup>114</sup> From the deregulated London markets these so-called "Eurodollars" were often lent forward to the developing countries. Due to a lack of control, the Eurodollars were frequently used to finance bad investments or robbed by corrupted dictators, thus planting the first seeds of the debt crisis.<sup>115</sup>

While the alterations in the operational environment explain a part of the change in the US relationship with the IFIs, domestic politics had surely a part to play as well. As the 1970s progressed, a strong faction supporting more nationalist foreign policy emerged in US politics. Overall, the confidence in a global rules-based system and in the power of multilateral organisations had waned.<sup>116</sup> Babb divides the protests of Congress into three groups "broadly corresponding to three major justifications for foreign aid: strategic, economic and humanitarian"<sup>117</sup>.

The first group was represented by those who had become disillusioned about the usefulness of development in the bipolar layout of the Cold War political environment. This argument was fuelled by countries like India, which were receiving substantial amount of aid but still regarded the US government with disdain. The second argument was drawn on populist rhetoric. According to it, US taxpayer's dollars were being spent lavishly on default and corrupted regimes in the developing countries. The third line questioned the humanitarian benefit of aid, maintaining that the money was not channelled effectively to the poor people, but rather, supported despots who did not respect the human rights of their citizens.<sup>118</sup>

Due to a resistant Congress, the second half of the 1970s witnessed an increase in the use of the "donor leverage" tactic. Withholding appropriations became a common strategy for the US Congress.<sup>119</sup> After the first IDA replenishment, every single one has stirred

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<sup>113</sup> Babb 2009, 103.

<sup>114</sup> Blyth 2002, 128–129.

<sup>115</sup> Ylönen 2012, 54–55.

<sup>116</sup> Kahler 1990, 98–99.

<sup>117</sup> Babb 2009, 61.

<sup>118</sup> Babb 2009, 61–64.

<sup>119</sup> Babb 2009, 67–68.

opposition in Congress. However, it was not until the Reagan administration came to power that the US government started to use the defiant Congress more openly in order to push for policy demands.<sup>120</sup>

Irrespective of the congressional opposition the Bank was able to increase its autonomy in the 1970s. McNamara had worked as the Secretary of Defence under John F. Kennedy (1961–1963) and Lyndon B. Johnson (1963–1969) and he had good connections to Congress, especially to the Democratic side of the aisle. Stern confirms that “Bob could and did influence congressional support”<sup>121</sup>. Moreover, the president of the Bank was respected in the larger US establishment as a visionary in development issues.<sup>122</sup> This newfound sense of respect undoubtedly enhanced the independence of the Bank. US bilateral aid was formulated according to the same lines as the Bank’s with poverty alleviation and rural development in the centre of attention.<sup>123</sup>

In my opinion, the US position regarding the Bank in this transitional period seems somewhat ambiguous. On the one hand, a growing opposition in Congress regarded the Bank and other multilateral organisations as an unending drain on money. On the other hand, the Bank’s new reorientation in tackling poverty was accepted in the US administration. The Bank was no longer viewed as a dysfunctional commercial Bank but as a credible forerunner in the field of development economics.

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<sup>120</sup> Ascher 1990, 125–126; Babb 2009, 115–121.

<sup>121</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Second session, 32. World Bank Group, Oral History Program.

<sup>122</sup> Ascher 1990, 121.

<sup>123</sup> Ascher 1990, 121.

## 2.4 The Neoliberal Breakthrough

By the 1970s Keynesian economics was under attack on several fronts. After years of booming global economic growth, a slowdown coincided with high rates of inflation and swelling unemployment. Keynesian economic policy, based on the principle of controlling inflation and the unemployment rate by stimulating domestic demand, was unable to tackle the new state of affairs. The loudest criticisms arose from a group of economists centred in the University of Chicago<sup>124</sup>, and led by the charismatic apostle of free markets, Milton Friedman. The adherents of the Chicago school viewed monetary policy as the appropriate tool for fighting stagflation. According to monetarist principles, central banks are able to control inflation simply by contracting and increasing the supply of money<sup>125</sup>.

The neoliberal program extends beyond the instrumental role it ascribes to monetarism. A second pillar of this rather heterogeneous ideological current is an unwavering belief in the freedom of individuals and markets. This conviction is based on rational choice theory at the individual level, and on the might of the price mechanism in organising markets. As a consequence, neoliberalist ideals attribute a minimal role to governments. The policy prescriptions of neoliberals can be crudely summarised by deregulation, privatisation and liberalisation.<sup>126</sup> As the name, neoliberalism, suggests, the origins of economic liberalism lie further back in history, namely in the classical liberal tradition of the 18<sup>th</sup> and 19<sup>th</sup> centuries, formulated in the writings of Adam Smith and other philosophers. Today, the term, neoliberalism, carries various connotations in different times and places. It was not commonly in use before the 1990s, and in the US, it often refers to a progressive liberal worldview.<sup>127</sup>

Jamie Peck captures wonderfully the quintessential nature of neoliberalism in the first pages of his book *Constructions of Neoliberal Reason*. According to him, neoliberalism can never exist in a truly pure form. Moreover, it is this inbuilt contradiction that actually defines it:

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<sup>124</sup> In this study, the “Chicago school” refers to the school of economic thought, not the actual educational institute.

<sup>125</sup> Desai 2013, 9.

<sup>126</sup> Ylönen 2012, 42.

<sup>127</sup> Mirowski & Plehwe 2009, 2; Peck 2010, 1–2, 13.

“Its utopian vision of a free society and free economy is ultimately unrealizable. Yet the pristine clarity of its ideological apparition, the *free market*, coupled with the endless frustrations borne of the inevitable failure to arrive at this elusive destination, nevertheless confer a significant degree of forward momentum on the neoliberal project. Ironically, neoliberalism possesses a progressive, forward-leaning dynamic by virtue of the very *unattainability* of its idealized destination.”<sup>128</sup>

Encapsulating the true essence of neoliberalism is not the goal of this investigation. In fact, Peck prefers to use the term neoliberalization, which refers to the process where the ideals of neoliberalism shape economic policies. In his own words:

“In the most abstract of terms, one can say that neoliberalization refers to a contradictory process of market-like rule, principally negotiated at the boundaries of the state, and occupying the ideological space defined by a (broadly) sympathetic critique of nineteenth-century laissez-faire and deep antipathies to collectivist, planned, and socialized modes of government, especially those associated with Keynesianism and developmentalism.”<sup>129</sup>

Peck argues that neoliberalization is not really concerned about diminishing the role the state: “notwithstanding its trademark antistatist rhetoric, neoliberalism was always concerned – at its philosophical, political and practical core – with the challenge of first seizing and then retasking the state”<sup>130</sup> In the process state resources are diverted from soft areas, like social care for example, to the likes of military spending. In fact, neoliberalism has forged intimate relationships with authoritarian regimes, most notably in Chile.<sup>131</sup>

The rise of neoliberalism is often portrayed as a revolutionary moment in time. Stedman Jones calls attention to two common narratives that are widespread in accounts on the spread of the economic ideology. The first one presents the emergence of neoliberalism as inevitable. In this narrative Keynesian economics is swept away suddenly and decisively by the mighty forces of neoliberalism. The reality is more nuanced. The neoliberal collective had carefully formulated their ideas during at least four decades of intense debate on both sides and across the Atlantic. Jones highlights the importance of

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<sup>128</sup> Peck 2010, 7. (Italics not added.)

<sup>129</sup> Peck 2010, 20.

<sup>130</sup> Peck 2010, 4.

<sup>131</sup> The case of Chile is well documented, even though the extent of Milton Friedman’s direct involvement is hotly contested. The disciples of Friedman advised the dictator Augusto Pinochet in formulating his economic policies with devastating consequences for the poorest part of the population. In 1988, when the stabilisation process in Chile was complete and the economy was growing at a fast pace, approximately 45 per cent of the population had been dragged into poverty. It is estimated that during Pinochet’s reign 3200 political dissidents disappeared or were killed, 80 000 imprisoned and 200 000 escaped the country. (Klein 2008, 77, 86).



the transatlantic networks in formulating neoliberal thinking.<sup>132</sup> While Friedman is rightfully credited as the popularising star of the movement, the true founding father of neoliberalism is thought to be Friedrich Hayek. The Austrian economist and philosopher founded the Mont Pelerin Society<sup>133</sup> in 1947 to counter the forces of “collectivism”.<sup>134</sup>

The second narrative is popular among the critics of neoliberalism. In these accounts the spread of neoliberalism is reduced to US imperialism and the Washington Consensus becomes a synonym to it.<sup>135</sup> Jones acknowledges that often “such analyses contain valuable insights”<sup>136</sup>. However, he argues that while neoliberalism has forged strong links with conservative politics and corporate power especially, it has been far more adaptive. The design of neoliberal policies has not been an exclusive right of conservatives. For example, the Democratic administration of President Jimmy Carter (1977–1981) started deregulating different sectors of the economy and appointed the monetarist Paul Volcker (1979–1987) as the chairman of the Federal Reserve (Fed).<sup>137</sup>

Friedman believed in the power of ideas and this is what made him such a formidable propagator of neoliberalism. He did not shy away from taking part in public debate. Thus, he took on two roles: “issuing audacious and uncompromising policy advice on the one hand, while fiercely protecting his reputation as an empirically oriented economist on the other”<sup>138</sup>. While Friedman established his place as the loudest advocate of neoliberalism, he was greatly assisted in this task by a new institutional innovation, the think tank. On both sides of the Atlantic, newly founded think tanks formed a network that disseminated the ideas that had started to take shape in Mont Pelerin.<sup>139</sup> In addition to academics, think tanks included businessmen, fundraisers, journalists and politicians.<sup>140</sup> Think tanks had a pivotal role in helping “turn neoliberal thought into a neoliberal political program”<sup>141</sup>. In the US, the most prominent neoliberal think tanks, the Heritage Foundation and the Cato

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<sup>132</sup> Jones 2012, 336.

<sup>133</sup> The Mont Pelerin Society is a club of liberal and conservative intellectuals. The founding fathers of the society included Hayek, Friedman, Karl Popper and Ludwig von Mises. (Mirowski & Plehwe 2009, 13, )

<sup>134</sup> Jones 2012, 32.

<sup>135</sup> Jones 2012, 12–14.

<sup>136</sup> Jones 2012, 14.

<sup>137</sup> Jones 2012, 5, 13. The Federal Reserve is the central bank of the US.

<sup>138</sup> Peck 2010, 97.

<sup>139</sup> Mirowski & Plehwe 2009, 5.

<sup>140</sup> Jones 2012, 134; Mirowski & Plehwe 2009, 6.

<sup>141</sup> Jones 2012, 135.

Institute were founded in 1973 and 1977 respectively.<sup>142</sup> These two had a profound influence on Republican politics during the next decade.<sup>143</sup>

On both sides of the Atlantic, it was an alliance with conservatives that lifted neoliberal policies into the limelight. In addition to the economic aspects of conservative neoliberal politics, Jones notes two other features that were interwoven in the alliance: a hostility towards Soviet communism and a reaction against the “so-called permissive society that was epitomized by the upheavals of 1968”<sup>144</sup>. While the conservative US and UK administrations did forge close links (Ronald Reagan and Margaret Thatcher got along famously well), the neoliberalizing process had different aspects in the two countries. In the UK, government policies attacked trade unions especially hard, while, in the US, neoliberalization facilitated the merge of government policies with the interests of big corporate business.<sup>145</sup> The rapid process of neoliberalization brought an end to the marginalisation of its proponents. In a sense, neoliberalism lost its sharpest ideological edge when it became “mainstreamed” and institutionalised in the conservative politics of the 1980s.<sup>146</sup>

The partnership with conservative political powers uncovers a few fundamental aspects of neoliberalism. The first is the fact that neoliberalism feeds out of crises. By and large, it was the crises of the international monetary regime and subsequent economic hardships that brought it into ascendancy. Moreover, Peck, Nik Theodore and Neil Brenner argue that neoliberalism has the ability to create crises for itself to exploit.<sup>147</sup> This observation provides an interesting perspective when analysing the most recent financial crash of 2008. The second central characteristic is the parasitic nature of neoliberalism. Neoliberalization gathers momentum by tangling with state power: “neoliberalism invariably exists in an essentially parasitical relationship with those extant social formations with which it has an antagonistic relationship, such as state socialism, social democracy, or neoconservative authoritarianism.”<sup>148</sup>

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<sup>142</sup> Jones 2012, 162–165.

<sup>143</sup> Babb 2009, 73.

<sup>144</sup> Jones 2012, 15.

<sup>145</sup> Jones 2012, 18.

<sup>146</sup> Peck 2010, 116.

<sup>147</sup> Peck, Theodore & Brenner 2010, 104.

<sup>148</sup> Peck, Theodore & Brenner 2010, 105–106.

I am inclined to believe that neoliberalism derives at least a portion of its power from its ideological impetus. While Keynesian economics did forge strong unions with political movements, social democratic forces in particular, one could argue that it still lacked the ideologically charged utopian features of neoliberalism. In hindsight, one must also note that Friedman's political activity has left a mark on the field of economics in a more comprehensive way. Today, economists are notoriously careful in formulating specific policy advices. It is the tendency of both economists and politicians to treat economics and politics as two distinct subject matters. Instead of promoting a healthy debate in the public sphere, economic policy is more often than not presented as if there were no alternatives to it. The reasons for this change are undoubtedly complex and plentiful, but, instinctively thinking, the controversial legacy of Friedman and his associates has surely had an impact on the transition.

In spite of the reluctance to make clear policy prescriptions, economists have undoubtedly been able to influence global affairs greatly. This point is underscored by Robert Chernomas and Ian Hudson in their book *The Profit Doctrine: Economists of the Neoliberal Era*. They argue, that after the neoliberal breakthrough, many of the leading economists that "rose to prominence...did so not because of their contributions to the standard list of economic goals, but primarily because of their contribution to corporate profit and the wealth of the business class"<sup>149</sup>. So, while a direct relationship linking academic economists and political policymakers has deliberately been downplayed, a tight union has nevertheless been forged between them, with the interests of big corporate business being the facilitator and a third party in the pact. The losers in this shift have been organised labour and the poorer tiers of society as the escalating income disparities, for example in the US, testify.<sup>150</sup>

Tracing a shift in the ideological orientation within the IFIs staffs is a tricky task. In a multilateral and outwardly neutral institution, staff members are careful about identifying themselves as followers of particular ideological doctrines. Due to the Bank's emphasis on broader development issues, it has historically had workers with more diverse backgrounds. This fact, together with the availability of analytically richer sources, has tilted my analysis of the spread of neoliberalism in the IFIs once again towards the Bank.

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<sup>149</sup> Chernomas & Hudson 2016, 2.

<sup>150</sup> World Bank Open Data, 16 January 2019. *GINI index (World Bank estimate): United States*.

The same holds true when I conclude this chapter by investigating the relationship between the IFIs and the influence of the Reagan government. As I stressed in the introduction, this bias is justified by the similarity of the institutions and the commonly held view that the Bank has been more sovereign with regard to the US.

A former employee of the Bank recalls how staff members worked side-by-side in the 1970s under Hollis Chenery (McNamara's right-hand man in development economics) irrespective of their ideological beliefs: "we had Marxists, we had structuralists, we had Chicago types, we had Keynesians, we had supply-siders. There was a bubbling and a very lively intellectual atmosphere"<sup>151</sup>. The intellectual diversity did not last long, however, as neoliberal approaches became predominant in the policies of the institutions in the wake of the debt crisis. Ernest Stern, a very influential figure in the Bank during the 1980s, is careful in defining his own intellectual positioning. However, trained in neoclassical<sup>152</sup> economics, he confesses that, in earlier years, the clear isolation of development economics did puzzle him somewhat:

"It was never very clear to me why development economics completely ignored the neo-classical rules of pricing and markets. Why wouldn't these concepts be relevant to the developing countries? That was always an issue floating in my mind. The current paradigm is, essentially, a rediscovery that some of the rules of normal economic theory apply to developing countries; that they are not exempt"<sup>153</sup>

This extract is by no means controversial and most economists today would indeed agree with Stern's statement. Nevertheless, I believe that some valuable insights can be drawn from it when the larger context is taken into account. Firstly, it has to be noted that the interview was conducted at the turn of the year in 1994–1995 when Stern was retiring after almost 25 years of service in the Bank. Even though his bafflement dates back to his early years in the institution, one gets a feeling that Stern is justifying to some extent a later change that occurred in the Bank's intellectual orientation. Secondly, it is important to highlight the weight of Stern's personal views. After McNamara left the Bank in 1981, the US government elected A.W. Clausen (1981–1986), the president of the Bank of

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<sup>151</sup> Interview with Attila Karaosmanoglu, 17 November 1994, 17. World Bank Group, Oral History Program.

<sup>152</sup> Neoclassical economics and neoliberalism are frequently used as substitutable terms, but the two should not be conflated. Broadly speaking, neoliberalism draws many of its core principles from neoclassical economics but differs from it essentially by carrying political and ideological implications. (Investopedia 30 June 2015.)

<sup>153</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: First session, 20. World Bank Group, Oral History Program.

America, as the new man in charge. Under his management a great deal of operational power was centralised in the hands of Stern.<sup>154</sup> The concentration of power overlapped with an expansion of structural adjustment lending in the adoption of which Stern had a crucial role.<sup>155</sup>

The IFIs gradual implementation of neoliberal economic policies coincided with a similar transition in American politics as Ronald Reagan took office in 1981. The parallel timing is hardly surprising considering the strong American influence in the IFIs detected in this study so far. While unearthing a far-reaching American agenda behind this process is virtually impossible, some indicators of US influence can be observed, most notably in the appointment of top management personnel in the IFIs.

Ngairé Woods maintains that when appointing senior staff members “the approval of United States is *de facto* necessary”<sup>156</sup>. Looking back at his time as the president of the Bank, Clausen recalls how “there was pressure from Treasury for key appointments”<sup>157</sup>. This was the case in 1982 when Anne Krueger was selected as the Bank’s chief economist, a position that carries probably the most ideological clout in the institution. Krueger was considered a conservative and had close ties to the American government, “very much hand-in-glove with the U.S. Treasury”<sup>158</sup>, as Shahid Husain – one of the vice-presidents at the time – frankly puts it. It is clear that Husain was not on the same wavelength with Krueger:

”Anne’s theory was that the market was supreme. In her view, the state should allow markets to work. It should not actively seek to eliminate poverty and income inequalities. More importantly, she also initiated a process of “ethnic cleansing” within the Bank. She got rid of anybody who had been associated with Hollis Chenery.<sup>159</sup>

While Husain’s views seem somewhat exaggerated, Ylönen is another who likens the arrival of Krueger to a purge, since employees who did not adhere to the neoclassical

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<sup>154</sup> Interview with Edward V. K. Jaycox, 23 February, 9 March, 27 April and 24 May 1995: Third session, 6-7; Interview with Syed Shahid Husain, 18 March, 20 April and 14 June 1994, 33-34; Interview with Benjamin B. King, 14 August, 16 and 21 October 1991, 67. World Bank Group, Oral History Program.

<sup>155</sup> Ylönen 2012, 44; Interview with Warren C. Baum, 13 November 1990, 31. World Bank Group, Oral History Program

<sup>156</sup> Woods 2003, 109. (Italics not added.)

<sup>157</sup> Interview with A. W. Clausen, 8 June 1992, 40. World Bank Group, Oral History Program.

<sup>158</sup> Interview with Syed Shahid Husain, 18 March, 20 April and 14 June 1994, 31. World Bank Group, Oral History Program.

<sup>159</sup> Interview with Syed Shahid Husain, 18 March, 20 April and 14 June 1994, 31-32. World Bank Group, Oral History Program.

paradigms of economics either left or were forced out. In the three years that followed Krueger's entry, 80 percent of the Development Research Group's staff had gone.<sup>160</sup> While acknowledging that "a lot of people complained about her management style"<sup>161</sup>, Stern valued Krueger's input: "she was a great asset to have around this period when we focused increasingly on adjustment programs, trade liberalization, macroeconomic conditionality, and relations with the Fund"<sup>162</sup>. Krueger herself highlights in a relatively recent interview that "almost everything I did was committed to development, which is committed, of course, to poverty reduction"<sup>163</sup>. However, she follows the claim by stating that "you cannot achieve very much in poverty reduction without getting reasonable economic growth"<sup>164</sup>. This is the most ideologically charged passage of a deliberately apolitical interview.

The Bank's focus on development issues had widened the organisation's occupational base, but by the 1980s economists were taking over the institution. This was a concern to Chenery who left the Bank the same year Krueger arrived.<sup>165</sup> Even Stern remarks that "structural adjustment lending boosted the role of the economists greatly – more than intended perhaps"<sup>166</sup>. One factor that facilitated the turn towards homogeneity in the institutions was the increasingly similar educational background of the workforce. David Knox, a regional vice-president of the Bank in the 1980s, describes the phenomenon:

"There was this deliberate effort to widen the geographical spread. I think that was good, but it had one serious drawback: almost all of these people we recruited came out of the same university background. They were almost all graduates of the main graduate schools in the United States or the U.K. or Western Europe, and while they may have come from Asia, Africa, Latin America, or wherever, their intellectual equipment with which they arrived was the intellectual equipment they had acquired in this very comparatively small number of graduate schools. So we didn't get a great deal of diversification."<sup>167</sup>

The numbers support Knox's statement. By 1991, 80 percent of the Bank's senior staff had graduated from Anglo-Saxon universities. Likewise, the staff of the Fund became

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<sup>160</sup> Ylönen 2012, 47.

<sup>161</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Third session, 50. World Bank Group, Oral History Program.

<sup>162</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Third session, 50. World Bank Group, Oral History Program.

<sup>163</sup> Interview with Anne O. Krueger, 29 January 2010, 8. World Bank Group, Oral History Program.

<sup>164</sup> Interview with Anne O. Krueger, 29 January 2010, 8. World Bank Group, Oral History Program.

<sup>165</sup> Interview with Hollis Chenery, 27 January 1983, 16. World Bank Group, Oral History Program.

<sup>166</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Third session, 26. World Bank Group, Oral History Program.

<sup>167</sup> Interview with David Knox, 21 May 1992, 17. World Bank Group, Oral History Program.

dominated by the alumni of North American graduate schools, as 90 percent of workers had graduated from American or Canadian universities in 1996.<sup>168</sup>

In my opinion the two facts – a general increase in the number and importance of economists and the pattern of geographic concentration in educational backgrounds – have both likely contributed to the proliferation of neoliberal thought and policies in the IFIs. While detecting direct American influence in this process is hard, it is safe to assume that they did not oppose the doctrinal transition and most likely contributed to it significantly. The American guidance is noticeable when hiring senior managers, as the case of Krueger highlights. While Woods notes that “staffing may not reflect the sociological view that knowledge is controlled to ensure a particular orthodoxy is imposed worldwide”<sup>169</sup>, I agree with her assessment that “a change in the politically appointed senior management in either institution can quickly redirect and underline a particular political mind set and blueprint for conditionality within the institutions”<sup>170</sup>.

## **2.5 From Cool Relations to Close Co-operation**

After a period of increased autonomy, US influence on the IFIs was strengthened as the 1980s passed. The tightening grip on both institutions was facilitated by an external shock: the onset of the debt crisis in Mexico in the autumn of 1982. Under Paul Volcker the Fed followed monetarist principles in tackling high domestic inflation. The hikes in interest rates – commonly known as the Volcker shock<sup>171</sup> – had damaging global effects in the developing countries which had borrowed excessively from private banks in the preceding decade, often in dollar-denominated loans. The debt crisis piled pressure on the Reagan administration because many of the banks that risked default were American and a global financial collapse loomed in the horizon.<sup>172</sup>

The debt crisis prompted a change in the American policy towards the Fund which had been marginalised under previous governments. The Reagan administration had initially

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<sup>168</sup> Woods 2003, 109.

<sup>169</sup> Woods 2003, 109.

<sup>170</sup> Woods 2003, 110.

<sup>171</sup> The interest rates peaked at 21 per cent in 1981 and remained at a high level through most of the 1980s. (Klein 2008, 159).

<sup>172</sup> Babb 2009, 106–107.

considered the Fund (and the Bank for that matter) as a financial burden but being a multilateral financial institution it proved a handy tool in confronting the crisis.<sup>173</sup> From the Fund's point of view, the debt crisis was a big opportunity to boost its prestige after difficult years.<sup>174</sup> With American support the Fund became a co-ordinator of sorts. Miles Kahler describes the change: "to ensure adequate financing for successful adjustment programs, the Fund became the linchpin in constructing financing packages for the major debtors"<sup>175</sup>. The new American line was supported by other major industrialised countries, namely Japan, Germany and the UK.<sup>176</sup> The alliance was consolidated in 1983, when the US government was able to persuade a resilient Congress to pass a 50 percent increase in the Fund's budget.<sup>177</sup> Underlying this change was an "activist"<sup>178</sup> executive manager of the Fund, Jacques De Larosi re (1978-1987). Under the Frenchman the Fund extended its involvement in the very poorest developing countries, especially in Sub-Saharan Africa after the second oil crisis of 1979.<sup>179</sup>

The US government did not, however, simply offer an enhanced role to the Fund with no strings attached. The Reagan administration, with its novel emphasis on the might of market solutions, pushed for policies that promoted fast structural adjustment in the developing countries in order to minimise their dependence on international interventions.<sup>180</sup> The American approach can be summarised to a "need for tightened conditionality in all Fund programs as well as an emphasis on the short-term nature of lending"<sup>181</sup>. Stress on the latter reveals that the Americans viewed the debt crisis essentially as a problem of liquidity.

While an acute catastrophe in the international banking system was averted, the debt crisis spread rapidly into many developing countries, especially in Latin America and Africa. The Bank had ongoing lending operations in many of these countries and it was thus drawn into the fold. The Reagan government had an interest in getting the Bank involved, since it wanted to restrict the Fund's operations to short term adjustment lending.<sup>182</sup> The

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<sup>173</sup> Kahler 1990, 103–104.

<sup>174</sup> Woods 2003, 94.

<sup>175</sup> Kahler 1990, 106.

<sup>176</sup> Kahler 1990, 105.

<sup>177</sup> Babb 2009, 107–108.

<sup>178</sup> Kahler 1990, 103.

<sup>179</sup> Kahler 1990, 103–104.

<sup>180</sup> Kahler 1990, 105–106.

<sup>181</sup> Kahler 1990, 106.

<sup>182</sup> Kahler 1990, 104.



Americans also wanted the Bank's project lending to meet stricter standards in struggling developing countries. This meant tightening conditionality in project loans and an increased emphasis on the selection of suitable projects in the first place.<sup>183</sup> These policies went hand in hand with stressing the importance of the private sector, as a lengthy but revealing paragraph from Attila Karaosmanoglu, a vice-president of the Bank in the 1980s, demonstrates:

"The prominence of the private sector, of course, raised also many policy issues. Now, all our lending operations have to be in conformity with the functioning of a market-based system and hence supportive of a healthy private sector. When we decided that the financial markets were not functioning properly, lending operations could only be supported in conjunction with a reorganization of the financial sectors relying on positive real interest rates. This meant that all those projects dried up. Yet, there may be instances where a power project or an oil project makes sense even if the markets are distorted. But we have ruled that out completely. I used to lose sleep over some of these issues."<sup>184</sup>

I believe that this extract illuminates the profound changes that were taking place in the IFIs in the 1980s. In a sense, the entire context of lending operations altered. Two different factors weighed in the process: an acute debt crisis and a change in the academic orthodoxy of economics which reflected itself in economic policies. This resulted in a fixation on the macroeconomic environment of the borrowing countries. In a sense, adjustment was seen as the only way out since the macroeconomic stability of the economy was the top priority. As a consequence, the IFI's lending operations became more politicised. To be sure, political considerations had influenced operations in earlier years, but now a market-based system relying on the private sector was a prerequisite for receiving aid.

While the Bank's project lending was tied down by new restrictions, program lending, especially in the form of SALs, was expanding. As mentioned earlier, a 10 percent cap in the Bank's overall lending volume had been imposed on the SALs when they were first adopted. However, a new way was quickly devised to circumvent the limit. This was done by issuing sectoral adjustment loans, focused on specific sectors of the economy, agriculture for example. A former employee of the Bank admits that "in a sense they were smuggled in"<sup>185</sup>. What is more, although project loans remained as the "bread and butter"

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<sup>183</sup> Babb 2009, 115–116.

<sup>184</sup> Interview with Attila Karaosmanoglu, 17 November 1994, 62. World Bank Group, Oral History Program.

<sup>185</sup> Interview with Vinod Dubey, 11 July 1994, 17. World Bank Group, Oral History Program.

of Bank operations, structural adjustment was getting most of the attention. Warren C. Baum, who retired from the Bank in 1986, offers his assessment of the lending volumes and explains the shift:

”And what I’m saying is that we continued to do 80 percent of our lending while we focused 75 percent of our attention on the 20 percent and allowed all of these other things to take place, and in this process we have done considerable damage to the institution.”<sup>186</sup>

Due to his departure, Baum does not consider himself to be in a position to evaluate the effectiveness of the SALs.<sup>187</sup> With damage he is referring here to the negligence of project lending. Nevertheless, it is clear that the Bank was heading towards uncharted waters with the increasing use of adjustment lending. While doing so, it was, in the view of many, also stepping on the toes of the Fund.

The relationship between the “Bretton Woods siblings”<sup>188</sup> has not always been rosy. From the very beginning, the institutions had distinct mandates but they often crossed paths when operating in the same countries. The interviews of the Bank’s former staff reveal that there has been a significant amount of contempt towards the Fund throughout the years.<sup>189</sup> Many people at the Bank felt that Fund officials had a rather superior attitude. Gerald Alter was the director of the Bank’s Western Hemisphere Department and the vice-president of the Latin American and Caribbean region in the 1960s and 1970s. His reminiscing dates back to the McNamara years:

”In some countries we had our differences, and the Fund was, of course, very, even at that stage, was very jealously guarding its jurisdiction. And when the chips were down, there were many people in the Fund that felt they could safely ignore what the Bank had to say.”<sup>190</sup>

Moreover, there are differences in the organisational cultures of the IFIs. Moeen Qureshi worked in both institutions and believes that the Fund, where he spent twelve years first, is characterised by a homogeneous working culture. Qureshi attributes this to three different factors: the majority of staff being economists, the European nature of the organisation and to the fact that most people have a background in working in central

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<sup>186</sup> Interview with Warren C. Baum, 13 November 1990, 32. World Bank Group, Oral History Program.

<sup>187</sup> Interview with Warren C. Baum, 13 November 1990, 32. World Bank Group, Oral History Program.

<sup>188</sup> Feinberg 1988, 547.

<sup>189</sup> Interview with Stanley Please, 26 August, 3; Interview with Aron Broches, 18 April and 23 May 1984: Second session, 17. World Bank Group, Oral History Program.

<sup>190</sup> Interview with Gerald Alter, 13 November 1990, 3. World Bank Group, Oral History Program.

banks or other financial institutions.<sup>191</sup> This homogeneity coupled with the fact that the Fund has been “historically dealing with a relatively narrow problem which could be solved in more or less the same or similar fashion”<sup>192</sup>, makes working in the Fund less multifaceted. In fact, the later senior vice-president of the Bank admits leaving the Fund because he was “intellectually bored”<sup>193</sup>. The flip side of the coin, according to many interviewees, is the efficiency of the Fund in comparison to the Bank where a heavier bureaucratic machinery tends to decelerate the decision-making process.<sup>194</sup>

In the 1980s it became apparent that the institutions’ operations were overlapping to a greater extent than before.<sup>195</sup> The debt crisis was a watershed in the relationship of the IFIs. Stern maintains that before it there was contact between the institutions “but the relations weren’t all that intimate”<sup>196</sup>. According to Stanley Please, at the onset of the debt crisis, “the whole question of Fund-Bank collaboration became very central right from the beginning”<sup>197</sup>. In his view, the Bank was not trespassing on the Fund’s territory, but rather, the institutions were both moving closer together with the mid-term time frame being the common denominator in the harsh financial conditions of the 1980s:

”The Bank had to relate its longer-term concerns to the medium-term horizon, the medium-term, liability in particular being the balance of payments. In effect, the Bank was altering its focus, not forgetting the longer-term focus, but also bringing its focus down to the medium-term. Whereas the Fund for its part was moving its focus to the medium-term not doing away with short-term stabilization but also looking to the medium-term. The introduction of the Extended Fund Facility, the EFF, was a reflection of that, a reflection of the fact that stabilization had to be seen not in a one-year horizon but as a medium-term problem.”<sup>198</sup>

The Bank’s move towards the middle ground was more recent, epitomised by the adoption of SALs in 1979.<sup>199</sup> The Fund had taken similar steps after the collapse of the Bretton Woods system: the EFF was established in 1974. In effect, this meant that, in the 1980s, both institutions were “providing balance of payments loans, tranching over one to

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<sup>191</sup> Interview with Moeen Qureshi, 5 April 1991, 5. World Bank Group, Oral History Program.

<sup>192</sup> Interview with Moeen Qureshi, 5 April 1991, 5. World Bank Group, Oral History Program.

<sup>193</sup> Interview with Moeen Qureshi, 5 April 1991, 5. World Bank Group, Oral History Program.

<sup>194</sup> Interview with A. W. Clausen, 8 June 1992, 15. World Bank Group, Oral History Program; Interview with Barber B. Conable, 8 May and 19 August 1991, 20-21.

<sup>195</sup> Interview with Moeen Qureshi, 5 April 1991, 3. World Bank Group, Oral History Program.

<sup>196</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Second session, 33. World Bank Group, Oral History Program.

<sup>197</sup> Interview with Stanley Please, 26 August, 26. World Bank Group, Oral History Program.

<sup>198</sup> Interview with Stanley Please, 26 August, 26-27. World Bank Group, Oral History Program.

<sup>199</sup> Feinberg 1988, 549.

three years, with medium-term amortization periods”<sup>200</sup>. Qureshi maintains that the “debt problem in a sense is the tip of the iceberg”<sup>201</sup>. According to him, the IFI’s job is, essentially, to tackle the underlying structural problems of the economies from a holistic point of view, and this justifies the merger in the medium-term:

”So in that sense merely going ahead and trying to eke out the short-term balance of payments equilibrium, even if it could be achieved, is not going to be sustainable. Similarly, if you were to merely think in terms of trying to resolve the longer-term issues of where is this economy going to be ten years from now, you’re not going to be able to do it because the inflationary environment that you’re dealing with doesn’t allow for any rational decisions to be made.”<sup>202</sup>

Thus, in addition to a temporal merge, a great deal of integration happened at the level of substance as well. Richard Feinberg studied the program loans of both institutions back in 1988 and found a pattern of increasing coalescence.<sup>203</sup> A comparison of economic variables in loan programs showed that both institutions were crossing some of the initial boundaries that had been erected between them. For example, the Bank’s programs included exchange rate adjustments, whereas the Fund was engaging in subjects such as energy pricing.<sup>204</sup>

One sign of closer collaboration was the introduction of Policy Framework Papers (PFPs) in 1986. These were jointly prepared country-specific papers produced by the staffs of both institutions in co-operation with representatives from the governments of borrowing countries. The PFPs were designed especially to confront problems in Africa, because they were targeted at IDA countries.<sup>205</sup> The Reagan administration regarded the PFPs as a means of formalising the association of the IFIs.<sup>206</sup> The US government “had wanted a guarantee of formal cross-conditionality”<sup>207</sup> between the institutions, which in effect meant that a borrowing country could not receive loans from one of the IFIs if it had not met the conditions of the other. While no such assurance was made, Babb notes that the PFPs “marked a significant harmonization of the two organizations’ policies”<sup>208</sup>.

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<sup>200</sup> Feinberg 1988, 549.

<sup>201</sup> Interview with Moeen Qureshi, 5 April 1991, 4. World Bank Group, Oral History Program.

<sup>202</sup> Interview with Moeen Qureshi, 5 April 1991, 4. World Bank Group, Oral History Program.

<sup>203</sup> Feinberg 1988, 550-552.

<sup>204</sup> Feinberg, 1988, 550.

<sup>205</sup> Interview with Edward V. K. Jaycox, 23 February, 9 March, 27 April and 24 May 1995: Fourth session, 9.

<sup>206</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Second session, 34. World Bank Group, Oral History Program.

<sup>207</sup> Babb 2009, 139.

<sup>208</sup> Babb 2009, 140.

While official cross-conditionality was never endorsed, Feinberg notes that “many decisions are taken by management and staff outside of the formal board framework”<sup>209</sup>. He distinguishes three mechanisms that facilitate cross-conditionality between the IFIs. In addition to the most important form, “consultative cross-conditionality”, described above, Feinberg identifies “interdependent cross-conditionality” and “indirect financial linkages”. Interdependent cross-conditionality is a mechanism where the IFIs select common conditions that they deem vital, an adjustment in the exchange rate for example, and make them “a priori” conditions before the borrowing countries have received any loans at all. An indirect financial linkage becomes visible when one of the IFIs withholds a loan, and as a consequence the borrowing state cannot meet its financial commitments to the other institution. This mechanism works through more extensive financial linkages as well, namely when third-party financiers, commercial banks for instance, are involved in the financial network.<sup>210</sup>

After decades of gradual divergence, new formal and informal links were forged between the institutions. Krueger had recurring meetings with her counterparts from the Fund, and President Clausen of the Bank worked in close collaboration with the Fund’s executive manager De Larosi re and Fed’s chairman Volcker.<sup>211</sup> Likewise, the later president of the Bank, Barber Conable (1986–1991), met the executive manager of the Fund, Michel Camdessus (1987–2000) regularly once a month.<sup>212</sup> Conable provides a detailed account of the challenges in Fund-Bank relations and how the co-operation took place through the PFPs:

“The problems are not of cross-conditionality. They're problems of disagreement about facts or something of that sort, and we are always running into different assumptions on oil prices or something, and then our Boards get upset. But, you see, we also have more contact than we used to have. For instance, the policy framework papers provide a point of contact. I don't think they're terribly significant myself, but those are worked out on a tripartite basis; the government, the Fund, and the Bank work out the policy framework papers. And we discuss them, and a Fund man comes and listens to the discussion. And we send our conclusions over to them, and they act on them ultimately.”

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<sup>209</sup> Feinberg 1988, 553.

<sup>210</sup> Feinberg 1988, 554-556.

<sup>211</sup> Interview with Anne O. Krueger, 29 January 2010, 8. World Bank Group, Oral History Program; Interview with A. W. Clausen, 8 June 1992, 22. World Bank Group, Oral History Program.

<sup>212</sup> Interview with Barber B. Conable, 8 May and 19 August 1991, 29. World Bank Group, Oral History Program.

Conable goes on to note that the PFPs “have more relevance to the Fund”<sup>213</sup> because the Bank already has country-specific management strategies. In my opinion, hidden beneath his remarks is a rather obvious hierarchical order. It seems as if the Bank was consulted but the Fund always went first. Other sources verify the deduction. David Knox confirms that, despite the closer co-operation in designing SAPs, a pecking order remained: “Fund first, Bank next”<sup>214</sup>. It became customary for the Bank to “wait for borrowers to arrive at a lending agreement with the IMF before agreeing to its own loan program”<sup>215</sup>.

Moreover, the Fund proved to be uncompromising in holding onto the preferred sequence of action. For instance, Camdessus was “furious”<sup>216</sup> when the Bank moved ahead of the Fund and issued an adjustment loan for Argentina in 1987.<sup>217</sup> However, in spite of the PFPs granting the Fund a position of precedence, the Bank’s role was not confined to a passive follower as it was able to contribute to the substance of the loan programs. In fact, after the introduction of the PFPs, the Fund moved a step further from quick disbursements towards Bank-style structural adjustment lending for longer time periods.<sup>218</sup> This was facilitated by the establishment of the Fund’s Structural Adjustment Facility (SAF)<sup>219</sup> in 1986.<sup>220</sup>

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<sup>213</sup> Interview with Barber B. Conable, 8 May and 19 August 1991, 29. World Bank Group, Oral History Program.

<sup>214</sup> Interview with David Knox, 21 May 1992, 25. World Bank Group, Oral History Program.

<sup>215</sup> Babb 2009, 140.

<sup>216</sup> Interview with Barber B. Conable, 8 May and 19 August 1991, 28. World Bank Group, Oral History Program.

<sup>217</sup> Interview with Barber B. Conable, 8 May and 19 August 1991, 28. World Bank Group, Oral History Program.

<sup>218</sup> Ylönen 2012, 61.

<sup>219</sup> The SAF was replaced by the Enhanced Structural Adjustment Facility (ESAF) shortly after in 1987. The ESAF, in turn, functioned until 1999. It was substituted with the Poverty Reduction and Growth Facility (PRGF), highlighting the change of policy orientation in the Fund. (IMF website, 14 January 2019. *IMF Concessional Financing through the ESAF*.)

<sup>220</sup> Babb 2009, 140.

## 2.6 Building the Washington Consensus

The Reagan administration's policies towards the IFIs are characterised by a sense of ambiguity, even though a slow process of warming relations can be traced through the years. While the IFIs were initially seen as a waste of tax payer's dollars, many in the Reagan administration started to gradually view them as useful tools in promoting the "magic of the market place"<sup>221</sup>. The American endorsement of structural adjustment should be viewed in light of this underpinning contradiction. Stern emphasises the importance of the US government input and the tripartite discussions in the increased issuing of SALs by the Bank:

"It was in this period that Structural Adjustment Lending became an operational tool. The issues the Bank sought to address in those days – trade liberalization, price decontrol, the internal market, the foreign investment framework, energy pricing – became topics of discussion between the Bank and the IMF, and with the U.S. Government. The U.S. Government played a major role in the debt crisis from the outset because of the massive systemic risk to the banking system, particularly in the U.S. and Japan."<sup>222</sup>

However, largely due to the increased autonomy acquired under the previous president, the relationship between the Bank and the US government was much more strained compared to the Fund. Thus, because of the activist role which the US government assumed, the 1980s can be viewed as a struggle between an American push for control and the Bank's thrust to oppose it. The Americans employed different methods in their pursuit for authority.

The Bank's management had customarily channelled its unofficial links with the American government via the State Department, but in the 1980s, American pressure was exerted mainly by the Treasury. Although the Americans had put great hopes in Clausen, the new president of the Bank did not simply comply under pressure. The relationship between Clausen and the Secretary of Treasury, Don Regan (1981–1985), was particularly uneasy.<sup>223</sup> Clausen was trying to increase the Bank's capital but the US administration and Congress were opposed to it. In response, Clausen resisted American

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<sup>221</sup> Ylönen 2012, 58; Babb 2009, 109.

<sup>222</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Third session, 39. World Bank Group, Oral History Program.

<sup>223</sup> Interview with A. W. Clausen, 8 June 1992, 31, 40. World Bank Group, Oral History Program.

influence and this soured the relationship further.<sup>224</sup> The president of the Bank felt that the US administration was not working for the common good, quite the opposite:

“But I felt the most political pressure from the United States and if I were the United States I wouldn’t be doing that. That was my test on political pressure. Everybody’s going to ask, on the theory that if they don’t ask enough, they’re not going to get more than what they ask for. And so I can understand that. But where some pressure is put, when it defied logic for what was best for the World Bank or what was best for the world, then that’s political pressure. That’s, pure, pure selfishness.”<sup>225</sup>

A turning point in the tense dealings was seen when Reagan shuffled his administration after winning a second term in office. Clausen acknowledges the slow process of change but at the same time highlights the importance of personal relations: “I must say that as the administration progressed, it became more understanding. And oh what a difference a Secretary of the Treasury can make!”<sup>226</sup> The new man in charge of the Treasury was James Baker III. In general, he had a more benign view of the IFIs, and more importantly, he was a pragmatist compared to his predecessor, and thus more willing to co-operate with the IFIs.<sup>227</sup>

The new approach was materialised in the launch of the Baker Plan soon after the new Treasurer took office in October 1985. The US government sought for new ways to battle the debt crisis, which it increasingly viewed as a longer-term condition originating from underlying structural problems in the economies of the developing countries, not just as an acute liquidity crisis. Many had hoped for debt reduction for the struggling countries but it did not materialise in Baker’s new initiative.<sup>228</sup> The Baker Plan was not designed for African countries. It was catered for 15 heavily indebted middle-income countries, most of them in South America.<sup>229</sup> The reason for this is quite straightforward. Because of their size, the larger middle-income countries, Brazil and Mexico for example, posed the real threat to the international banking system. While smaller African economies were equally indebted, their default would not cause a catastrophic chain of events.<sup>230</sup>

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<sup>224</sup> Interview with Attila Karaosmanoglu, 17 November 1994, 66. World Bank Group, Oral History Program.

<sup>225</sup> Interview with A. W. Clausen, 8 June 1992, 31. World Bank Group, Oral History Program.

<sup>226</sup> Interview with A. W. Clausen, 8 June 1992, 31. World Bank Group, Oral History Program.

<sup>227</sup> Babb 2009, 132.

<sup>228</sup> Babb 2009, 128–129.

<sup>229</sup> Interview with A. W. Clausen, 8 June 1992, 24. World Bank Group, Oral History Program.

<sup>230</sup> Cline 1989, 1. *The Baker Plan: progress, shortcomings, and future (English)*. WPS 250. World Bank Archives.



However, analysing the Baker Plan is relevant for this study, because it reveals how the American government at the time viewed the debt crisis and the role of the IFIs in fighting it. Thus, it reflected the American stance more generally and had implications for all developing countries that were struggling with debts, many of them in Africa. Babb distinguishes the three main objectives of the Baker plan:

”First, debtor countries needed to adopt “comprehensive macro-economic and structural policies supported by the international financial institutions, to promote growth and balance of payments adjustment, and to reduce inflation.” Second, Baker called for “a continued central role for the IMF, in conjunction with increased and more effective structural adjustment lending by the multilateral development banks, both in support of the adoption by principal debtors of market-oriented policies for growth.” And, third, he proposed “increased lending by private banks in support of comprehensive economic adjustment programs“.”<sup>231</sup>

The first and the third elements had been central for the US since the onset of the crisis. The novel thing about the Baker Plan was that it wanted to increase the involvement of the multilateral development banks (MDBs), of which the World Bank was the most important financier.<sup>232</sup> Most notably, Baker wanted the development banks to issue quickly disbursing policy-loans to promote growth and exports, which in effect meant increased application of SAPs. In addition, the banks needed to tighten conditionality and increasingly focus on Fund-like policy prescriptions, exchange rate adjustments for example.<sup>233</sup> The PFPs were introduced after the launch of the Baker Plan as a tool for tightening the uniformity of the IFI’s policies.<sup>234</sup>

Another new aspect of the Baker Plan was the added emphasis on “market-oriented solutions”. Trade and capital liberalisation had been on the table longer but promoting the privatisation of state-owned companies was a new approach from Reagan’s administration. Babb emphasises the importance of this change as the US government wanted now to “use program lending as an incentive to get governments to divest themselves of public enterprises and, thereby, to launch a major transformation of the economic governance of developing countries”<sup>235</sup>. Furthermore, Babb summarises cleverly the American rationale behind the entire Baker Plan: “if growth was the only

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<sup>231</sup> Babb 2009, 128. Quotations from Montagnon, Peter: “*Baker’s Third World Debt Plan*”, Financial Times, 9 October 1985, section I.

<sup>232</sup> Babb 2009, 129. The other major development bank that was heavily involved in the debt crisis was the Inter-American Development Bank (IDB).

<sup>233</sup> Babb 2009, 129.

<sup>234</sup> Babb 2009, 139.

<sup>235</sup> Babb 2009, 130.

solution to the debt crisis and liberalizing reforms the only means toward growth, then it stood to reason that IFIs needed to be fully mobilised to promote liberalizing reforms”<sup>236</sup>. For the purpose of this study, the most important fact to draw from the Baker Plan is the significant change in American policy which it reflected. In essence, the IFIs were promised more funds by the American government, but the price was more extensive policy demands.

The Baker Plan signalled a change in the deployment of the administration’s most important channel of influence. The donor leverage tactic was used extensively under Reagan’s first administration because in addition to a sceptical Congress, the government itself regarded the multilateral institutions as ineffectual organisations.<sup>237</sup> The change of administration in 1985 did not usher the end of the tactic’s employment, but rather, after that, donor leverage was used more eagerly to push for preferred policies, not just for regulating the amount of capital allocated to the IFIs.<sup>238</sup>

Clausen considered the Baker Plan to be “a good idea”<sup>239</sup>, though he was not very pleased with the way in which the Americans prepared it without thoroughly consulting the IFIs.<sup>240</sup> Not everybody at the Bank, however, was convinced. David Knox recalls how a year after the launch of the initiative he was “already very concerned that we had just been overly optimistic, very, very optimistic”<sup>241</sup>. The private banks and the development banks failed to muster the proposed amount of capital and the rapid adjustment policies did not lift the economies out of the slump. In fact, the situation in most of the 15 countries deteriorated in the following years.<sup>242</sup>

Knox had started to promote debt reduction already in 1986, but at the time it was not seen as a viable policy option in the IFIs, quite the opposite. According to Knox, “the reaction in the Bank was one of horror, and the reaction in the Fund was even more”<sup>243</sup>. Knox laments the fact that while management in the Bank warmed gradually to the idea,

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<sup>236</sup> Babb 2009, 129.

<sup>237</sup> Babb 2009, 133.

<sup>238</sup> Babb 2009, 147.

<sup>239</sup> Interview with A. W. Clausen, 8 June 1992, 24. World Bank Group, Oral History Program.

<sup>240</sup> Interview with A. W. Clausen, 8 June 1992, 23-24. World Bank Group, Oral History Program.

<sup>241</sup> Interview with David Knox, 21 May 1992, 8. World Bank Group, Oral History Program.

<sup>242</sup> Heavily Indebted Countries (2) (Baker Monitoring), 1986–1987. Office Memorandum, Monitoring the Baker Plan, 2. 11/30/1987. IMF Archives.

<sup>243</sup> Interview with David Knox, 21 May 1992, 9. World Bank Group, Oral History Program.

shareholder pressure (mainly American in this case), slowed the process markedly.<sup>244</sup> It was not until George H.W. Bush took office in 1988 that debt reduction was finally approved as a possible means for solving the crisis. In the next year, the new US administration introduced the Brady Plan<sup>245</sup> which involved debt relief on a small scale.<sup>246</sup>

While Knox was frustrated with the slow process of change, more profound criticism was also evident at the Bank. Shahid Husain replaced Warren Baum as the vice-president of the Operational Policy Staff in 1983 and from then on was involved in the handling of the debt crisis. Husain wrote a report where he identified the debt crisis as a structural problem rather than a liquidity issue, as Krueger, the Fund and Volcker all maintained.<sup>247</sup> According to him, Stern blocked the paper from reaching the executive board and Husain's analysis was not taken into consideration.<sup>248</sup> The official view of the Bank changed with the introduction of the Baker Plan as structural problems were recognised behind the debt crisis, but in Husain's view a complete turnaround was not seen before a change in the US administration:

"After George [H. W.] Bush came to power, everybody finally recognized that the debt crisis was a structural issue and then the Bank fell in line. The Bank, intellectually, failed the developing countries and its constituents. It didn't even provide a decent analysis of the debt issue. The lead was clearly in the hands of the U.S. Treasury. The Bank and the IMF saw their role as simply following the U.S. Treasury's lead. That was the fundamental change that took place between the McNamara times and the post-McNamara times. On key issues, like the debt issue, the Bank had basically ignored its role as an independent thinker and as an independent propounder of policy. Instead, Krueger and Stern chose to limit the Bank's role to one of implementing the policies of the U.S. Treasury."<sup>249</sup>

Husain's views should be taken with a pinch of salt. First of all, he presents his story in a bitter tone, contempt towards some of his senior colleagues is obvious. Secondly, by the time of the interview it was clear that structural adjustment had not been a success story

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<sup>244</sup> Interview with David Knox, 21 May 1992, 9-10. World Bank Group, Oral History Program.

<sup>245</sup> The Brady Plan was named after the Secretary of Treasury Nicholas F. Brady (1988-1993). The central idea of the initiative was to give private lenders a set of options. Commercial banks had to choose between borrowing more money to an indebted country or changing their existing loans to it to "Brady bonds", which were guaranteed by the US. If they opted for the latter, the banks could then choose a market-based interest rate which lowered the total sum of the debt, or they could choose to hold on to the total sum, which in turn meant that a lower, fixed interest rate would be tied to it. (Ylönen 2012, 62-63.)

<sup>246</sup> Ylönen 2012, 62-63.

<sup>247</sup> Interview with Syed Shahid Husain, 18 March, 20 April and 14 June 1994, 32. World Bank Group, Oral History Program.

<sup>248</sup> Interview with Syed Shahid Husain, 18 March, 20 April and 14 June 1994, 33. World Bank Group, Oral History Program.

<sup>249</sup> Interview with Syed Shahid Husain, 18 March, 20 April and 14 June 1994, 33. World Bank Group, Oral History Program.

in most parts of the world. Nevertheless, Husain is right about the fact that the IFIs did lose a significant amount of their autonomy. I don't believe that the IFIs simply fell in line and followed the American lead. However, it is evident that substantial compromises were made in the process of getting an intellectually heterogeneous organisation, like the Bank, to co-operate closely with the conservative and profoundly pro-market administration of Ronald Reagan. Critical voices were forced out or marginalised, as the case of Husain proves.

The last years of the tumultuous 1980s were an especially difficult time for the Bank. After President Clausen was replaced by the Republican ex-congressman Conable in 1986, the Bank went through a reorganisation process the next year. As a result, 10 percent of the staff was laid off and many more were reshuffled inside the organisation.<sup>250</sup> In many ways the reorganisation had been coming for some time, because a lot of the power that was centralised under McNamara had moved to the hands of Stern and this was constraining the organisation.<sup>251</sup> Many of the Bank's former employees highlight the fact that an American initiative in bringing it about was significant.<sup>252</sup> Baum represents a commonly held view of the episode:

"Well in my mind a major purpose of the reorganization was to get Ernie out of the operation complex. I will give you my scenario, which you'll match against a hundred others to find where the truth lies, but when Conable came on board, he was picked by the [Ronald] Reagan team with a certain number of conditions. He wanted, he knew he had to get IDA replenishment, he knew he had to get a Bank capital increase. He was held hostage to the administration which appointed him. The price was: "You've got to streamline the operations of the Bank. You've got to do work faster. You've got to get rid of this redundant staff. You've got to get rid of all of these excess vice-presidents. You've got to get rid of Ernie Stern". And I think this was his brief when he came into the institution."<sup>253</sup>

Conable is vehemently opposed to the idea of the reorganisation being a plot machinated by the Americans.<sup>254</sup> According to the former president, he was actually the one to propose the idea to Baker first and to this the Treasurer replied: "well, that's something

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<sup>250</sup> Babb 2009, 139.

<sup>251</sup> Interview with Edward V. K. Jaycox, 23 February, 9 March, 27 April and 24 May 1995: Third session, 6-7; Interview with Benjamin B. King, 14 August, 16 and 21 October 1991, 67. World Bank Group, Oral History Program.

<sup>252</sup> Interview with Ernest Stern, 16 and 29 December 1994, and 5 January 1995: Fourth session, 12-13; Interview with Syed Shahid Husain, 18 March, 20 April and 14 June 1994, 34. World Bank Group, Oral History Program.

<sup>253</sup> Interview with Warren C. Baum, 13 November 1990, 15-16. World Bank Group, Oral History Program.

<sup>254</sup> Interview with Barber B. Conable, 8 May and 19 August 1991, 25. World Bank Group, Oral History Program.

you should consider, but I'm not telling you you've got to have one”<sup>255</sup>. However, highly relevant incidents had taken place before this point of time. In a rather bizarre chain of events, Baker had initially asked Conable’s permission to use the former congressman’s name in private discussions regarding the vacant presidency, without seriously proposing that he take the job. The Treasurer wanted to add Conable to the shortlist in order to eliminate unwanted candidates from the race.<sup>256</sup> Conable was in a state of shock when he found out that he was actually offered the presidency. Once again, he narrates the story by recounting his dialogue with the Treasurer: “My lord, Jim, this -- you can’t do this to me! I – this was not the understanding we had”<sup>257</sup>.

After reluctantly accepting the position, another twist was seen just two days before the new president of the Bank took office. The executive board rejected a new budget (submitted by the departing President Clausen), with US, Japan and France voting against it. At this point Conable felt that his hands were tied, and in order to secure the funds he suggested the reorganisation to Baker.<sup>258</sup> Unsurprisingly, once the reorganisation was under way the Executive Board approved the new budget.

Therefore, irrespective of the initial ownership of the idea, the American input behind the reorganisation was crucial. It is no coincidence that the Americans chose a seasoned political veteran to head the Bank shortly before the reorganisation. Moreover, with the threat of not securing new funds, the new leader of the Bank had little option but to somehow streamline the operations of the organisation. Quite evidently the reorganisation had full American support, and a trap of sorts was set for Conable so that he would have to implement it. Whether the reorganisation was the ultimate aim of the American administration remains inconsequential. The bottom line is that the US government viewed the Bank as an oversized organisation and was able to once again influence its fate.

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<sup>255</sup> Interview with Barber B. Conable, 8 May and 19 August 1991, 25. World Bank Group, Oral History Program.

<sup>256</sup> Interview with Barber B. Conable, 8 May and 19 August 1991, 2. World Bank Group, Oral History Program

<sup>257</sup> Interview with Barber B. Conable, 8 May and 19 August 1991, 3. World Bank Group, Oral History Program.

<sup>258</sup> Interview with Barber B. Conable, 8 May and 19 August 1991, 7. World Bank Group, Oral History Program.

In this light, the events leading to the reorganisation should be seen as a striking piece of evidence of a strong US authority at the time. By 1987 the US government had come to regard the IFIs as useful allies, and thus, an increased willingness on the part of the administration to push for control had emerged. Conable speaks of American authority openly: “Their interest is in maintaining hegemony here. Looking ahead with their tremendous shortfall of foreign aid money and the probability that it's going to get even tighter, they think it's terribly important that they control this institution”<sup>259</sup>.

After reading the rather cautious and vague interviews of the Bank's earlier top management in relation to American influence, a strikingly different tone is portrayed in the frank and uncompromising passages in which the presidents of the 1980s, Clausen and Conable, speak of direct US meddling.<sup>260</sup> I am inclined to ascribe this shift to an understandable aspiration on the behalf of the two presidents to hold on to a perceived autonomy of the Bank. US influence at the time was so obvious that denying it would be implausible and counterproductive. At that point in time, the US influence was in flux, moving from the strong, but relatively implicit, influence of earlier years to tighter, and crucially, more explicit influence as the 1980s progressed.

The gradually ripened understanding and co-operation between the US government and the IFIs was conceptualised in 1989, when the term Washington Consensus was coined by the sociologist John Williamson. With the term, Williamson referred to a set of market-liberalising policies negotiated between the IFIs and the US government. I will not go over the exact list of policies here, because a reasonably accurate picture of the economic prescriptions can be found in the two previous subchapters of this study. It is sufficient to quote Williamson:

“A striking fact about the list of policies on which Washington does have a collective view is that they all stem from classical mainstream economic theory...None of the ideas spawned by the development literature...plays any essential role in motivating the Washington Consensus.”<sup>261</sup>

Washington Consensus referred initially to policies directed at indebted Latin American countries, but its meaning rapidly broadened to include other developing countries of the

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<sup>259</sup> Interview with Barber B. Conable, 8 May and 19 August 1991, 35. World Bank Group, Oral History Program.

<sup>260</sup> Interview with A. W. Clausen, 8 June 1992, 31. World Bank Group, Oral History Program; Interview with Barber B. Conable, 8 May and 19 August 1991, 35. World Bank Group, Oral History Program.

<sup>261</sup> Babb 2009, 126–127. Quoted from Williamson, “*What Washington Means by Policy Reform*”, 19.

world as well.<sup>262</sup> Its intellectual and ideological background stemmed from the rejection of Keynesian economics and “Third World statism”<sup>263</sup>. However, Ylönen highlights the fact that “the Consensus was not just a political program or an academic doctrine, but a tool, with which economic and societal ideas were mobilised into action”<sup>264</sup>. These policy prescriptions were applied extensively in developing countries around the world during the 1980s and the 1990s.<sup>265</sup>

Back in 1989, Williamson was in his own words “oblivious to the thought that I might be coining either an oxymoron or a battle cry for ideological disputes for the next couple of decades”<sup>266</sup>. Certainly, in left-leaning circles, the Washington Consensus has become a swearword of sorts. It is often conflated together with ideas about neoliberalism and market fundamentalism, in such a way that Williamson, quite understandably, feels that the original meaning of the term is lost.<sup>267</sup> Taking note of this fact does not, however, diminish the valuable insights that some critical commentators have constructed by drawing upon the Washington Consensus as a conceptualisation. Particularly renowned are the works of a few economists critical of globalisation, Dani Rodrik and Joseph Stiglitz, the latter of whom was chosen as the Bank’s chief economist in 1997.<sup>268</sup>

Since the conception of the Washington Consensus, the IFIs have gradually distanced themselves from US government policies. While it is safe to assume that the need for change has stemmed mainly from the inadequacy of former policies, the ideological battle around the concept has surely contributed to the shift as well. Williamson argues that if the term is to be comprehended as an understanding between the US government and the IFIs, the “consensus has evaporated”<sup>269</sup>. From the 1990s onwards the IFIs have focused on matters like institution building and income distribution. The Bank has lifted good governance and fighting corruption to the centre of its agenda.<sup>270</sup> The IFIs launched the

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<sup>262</sup> Williamson 2004, 199-200.

<sup>263</sup> Babb 2009, 126.

<sup>264</sup> Ylönen 2012, 63. (Own translation.)

<sup>265</sup> Ylönen 2012, 63.

<sup>266</sup> Williamson 2004, 196.

<sup>267</sup> Williamson 2004, 201.

<sup>268</sup> Rodrik 2014; Stiglitz 2002.

<sup>269</sup> Williamson 2004, 201.

<sup>270</sup> Williamson 2004, 200.

Heavily Indebted Poor Countries (HIPC) initiative in 1996, which included debt relief to the very poorest countries of the world.<sup>271</sup>

Because of the limited range of this study, it is not possible or even necessary to examine thoroughly the various features of the concept. However, I feel that some important aspects of the Washington Consensus need to be emphasised. Although the term has its limits as a conceptualisation, and one often stumbles upon rather uncritical ways of applying it, I do find it useful for three reasons. First of all, the spatial connotations of the term should be highlighted. In addition to serving as the headquarters of the IFIs and the US government, Washington D.C. is also the home to many economic think tanks and development-oriented congressmen.<sup>272</sup> Thus, the Washington Consensus should be seen as a broader understanding spanning across multiple levels of governance, not just as a one-way push on the behalf of the US executive.

Secondly, it is important to view the Washington Consensus in the precise historical context of the time. I would argue that the world has grown more multipolar since and this has affected multilateral institutions profoundly. In contrast, thirty years ago globalisation was well under way, but the communist block was crumbling and China's remarkable economic growth was only beginning to gather momentum. Although history did not come to an end, as the political scientist Francis Fukuyama famously declared, a sense of an inevitable triumph of free markets can be traced in and around the years of the Washington Consensus.<sup>273</sup> I would argue that this led to overconfidence and backfired to some extent in many parts of the world that were introduced to the forces of free market capitalism. Aggressive SAPs were pushed through in many of the old Soviet states and communist countries, for example, with adverse outcomes.<sup>274</sup>

Thirdly, and most importantly in my opinion, it needs to be emphasised that the Washington Consensus was not born overnight. It was forged slowly as the US administration's stance on the IFIs changed from a hostile view to a pragmatic acceptance. Initially, the US government followed the line of the Heritage Foundation and other conservative think tanks in maintaining that the IFIs were unreliable organisations that funded socialist governments. This view was gradually pushed to the

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<sup>271</sup> Ylönen 2012, 170. Zambia is one of the 39 HIPC countries.

<sup>272</sup> Babb 2009, 126.

<sup>273</sup> Fukuyama 1992.

<sup>274</sup> A detailed account on Poland and Russia can be found in Klein 2008.



background, and the selection of James Baker as the Secretary of Treasury was a pivotal moment in this process.

The Fund was accepted as a credible collaborator faster, because it was better equipped to fight the debt crisis. In addition, it is safe to presume that the Fund's relatively limited focus on balance of payments issues and a rather homogenous workforce made it an easier partner for US officials. In order for the Bank to get involved, it had to win the US government's trust in its abilities to impose tough policy conditions.<sup>275</sup> The IFIs would not have engaged in structural adjustment lending on the same scale without the US government's influence and approval. Quite the contrary, the American contribution was vital. Babb encapsulates this well in noting that "the dramatic rise of structural adjustment among multilateral lenders was made possible by strong shareholder activism"<sup>276</sup>.

From the IFI's point of view, the 1980s were challenging but at the same time stimulating years. The Fund found a new sense of purpose after the marginalisation that had followed the end of the Bretton Woods system. The debt crisis legitimated its role as the "Band-Aid" of acute liquidity crises. In addition, it was able to diversify its lending operations greatly with the advent of SAPs. For the Bank the decade was a more ambivalent period. From the sociologically inspired organisational view, the Bank's increased policy-lending and co-operation with the US government made sense, although significant ideological opposition evidently grew within the institution. By forging close relations with the US Treasury, the Bank was able to secure funds and increase its budget, but the flip side of the coin was the American push for control.

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<sup>275</sup> Babb 2009, 135.

<sup>276</sup> Babb 2009, 145.

### 3. The Case of Zambia

#### 3.1 The Curse of Copper

In this chapter I will recount the economic history of postcolonial Zambia. To begin with, I will provide some essential basic information about the former British colony. I will also present a short summary of the fortunes of its mining industry, because the sector is vital in understanding the economic trajectory of Zambia. This section will be followed with a brief theoretical analysis that highlights the insecure position of Zambia as a small, open and undiversified economy. After the introduction, I will embark on a more detailed account of the Zambian economic path.

In order to comprehend Zambia's economic history, it is imperative to shed light on key political developments as well. Due to Zambia's precarious geopolitical location, foreign affairs – questions related to national security in particular – have had an important role in explaining its postcolonial history. Other important political dynamics include the state's relations with influential trade unions and the persistent opposition between the urban working class and rural people toiling in agriculture. However, for the purpose of this study, the main emphasis will lie on Zambia's relations with the IFIs. The aim is to juxtapose the evolution of the IFIs with the Zambian experience. The primary question is: how were American influence and the tightening conditionality in the IFIs reflected in the case of Zambia?

The Republic of Zambia was established on the 24 October in 1964 replacing the British protectorate of Northern Rhodesia. The struggle for independence was led by Kenneth Kaunda (1924–) and his socialist United National Independence Party (UNIP). Kaunda was inaugurated as the republic's first president. He consolidated his power in 1972 with a constitutional change that made Zambia effectively a one-party state. Nearly twenty years later Zambia was one of the earliest African states that went through a (relatively) calm transition to democracy. Kaunda was defeated in the free elections of 1991 by the Movement for Multi-Party Democracy (MMD) that had strong support from trade unions.

The leader of the MMD, Frederick Chiluba (1943–2011), was chosen as president and under his rule Zambia went through sweeping economic liberalisations in the 1990s.<sup>277</sup>

Zambia joined the IFIs in September 1965.<sup>278</sup> The newly established central bank, the Bank of Zambia (BoZ), issued the republic's first official currency, the Zambian pound, in 1964. A couple of years later the currency was switched to the Zambian kwacha, which was pegged to the British pound at a fixed rate of 1.7094 kwacha per pound. After the Nixon shock in August 1971, the kwacha was pegged to the American dollar.<sup>279</sup>

Although Zambia has an abundant supply of natural resources, its geographic location is not optimal in terms of international trade. It is a land-locked country with eight neighbouring states: The Democratic Republic of Congo, Angola, Namibia, Botswana, Zimbabwe, Mozambique, Malawi and Tanzania (see Figure 1, page 57). Thus, good relations with bordering states and functioning infrastructure are crucial for maximising the potential of exports, as well as bringing in imports. Zambia has a tropical climate that is moderated by elevation as the country sits on the plateau of Central Africa (roughly 1000-1600 meters above the sea level). The land in Zambia is very suitable for agriculture due to plentiful water reserves. Only one and a half million hectares is cultivated yearly of a land resource base of 42 million hectares<sup>280</sup>.

Resembling the familiar pattern of African demographic development, Zambia's postcolonial history has been characterised by fast population growth. When Zambia gained independence, the country had less than three and a half million inhabitants. During the next fifty years the population more than quadrupled to 16 million in 2015.<sup>281</sup> At its peak, the total fertility rate<sup>282</sup> was almost 7.4 in the 1970s. The fertility rate has fallen somewhat since, but in a global perspective it has remained very high, with Zambian women giving birth to nearly five children on average in 2016.<sup>283</sup> Unlike many other countries in the continent, Zambia has not suffered from civil wars. The AIDS-epidemic of the 1990s and early 2000s has been the biggest factor affecting mortality

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<sup>277</sup> Sardanis 2003, 155-157, 261-265; Fraser 2010, 10–11.

<sup>278</sup> IMF website, 23 January 2019. *List of Members*.

<sup>279</sup> Bank of Zambia website, 9 April 2019. *Currency History*.

<sup>280</sup> Zambia Development Agency website, 24 January 2019. *Agriculture*.

<sup>281</sup> World Bank Open Data, 10 January 2019. *Population, total: Zambia*.

<sup>282</sup> Total fertility rate is a demographic parameter that calculates the average amount of children a woman gives birth to in a population during her lifetime.

<sup>283</sup> World Bank Open Data, 10 January 2019. *Fertility rate, total (births per woman): Zambia*.

rates. The peak of the epidemic was seen back in 1996, when nearly 15 per cent of Zambian women aged 15–24 were infected by the HIV-virus. Today, AIDS is still an acute health issue, but prevalence has dropped to less than six per cent in the young female population.<sup>284</sup>

**Figure 1. Map of Zambia**



(Source: CIA, The World Factbook: Zambia.)

Rapid population growth has unquestionably had a considerable impact on the economic performance of the country. Blaming underdevelopment solely on population growth is, however, unjustified. After taking a closer look at the data, a more detailed picture is revealed. The Zambian population doubled in the first 22 years of independence. During this time GDP per capita (measured in constant 2010 dollars)<sup>285</sup> dropped from roughly 1500 dollars to approximately 1090 dollars in 1986 (the average level of income remained fairly stable at first, but a steep fall started in 1976). In spite of plummeting to a low of

<sup>284</sup> World Bank Open Data, 15 January 2019. *Prevalence of HIV, female (% ages 15-24): Zambia*.

<sup>285</sup> GDP per capita in constant prices measures historical incomes using the value of a certain year as a base, 2010 in this case. It is also known as real GDP per capita.

900 dollars in 1994, GDP per capita recovered back to 1500 dollars between 1986 and 2011. In these 25 years the population doubled again from roughly seven million to 14 million.<sup>286</sup> If population growth is taken as a foundational cause of poor economic performance, surely the decline in GDP per capita should have been more constant, instead of having the shape of a u-curve.

Moreover, fast but steadily declining population growth creates potential for future economic progress as the portion of young adults increases in relation to children and older people.<sup>287</sup> As for many other Sub-Saharan countries, the utilisation of this “demographic dividend” is a key question for Zambia in the coming decades. Most importantly, investments in health care and education are paramount, because a large and young population may also be a source of unrest if jobs and opportunities are scarce.<sup>288</sup>

Historically, Zambia’s urban population has been vast compared to other African countries. Moreover, urbanisation started very early in the region because of the expansion of the mining industry in the Copperbelt province during the 1930s and 1940s.<sup>289</sup> The Copperbelt is located 200 kilometres north of the capital Lusaka (see Figure 1). The province still has many large mining towns and has remained the most urbanised region in Zambia. Lusaka is by far the biggest city in the country, however, with approximately two and a half million residents in 2018.<sup>290</sup> The urban population of Zambia reached over one million in 1969 and at the time 750 000 Zambians worked in waged employment.<sup>291</sup> Today, 43 per cent of the total population dwell in urban areas, but an almost equal level was reached back in 1980.<sup>292</sup> The economic liberalisation of the 1990s contributed significantly to the growth of the informal economy as the public sector

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<sup>286</sup> World Bank Open Data, 18 January 2019. *Population total: Zambia*; World Bank Open Data, 18 January 2019. *GDP per capita (constant 2010 US\$): Zambia*.

<sup>287</sup> In demographic terms this factor is called the dependency ratio, which calculates the size of the working-age population in relation to children (aged 0-15) and older people (aged over 65). Because of the rapid population growth, the dependency ratio in Zambia has been very high throughout its postcolonial history, albeit a steady decline started about ten years ago. In many developed countries the trend is the opposite, Japan being a common example since it has a rapidly ageing population. (World Bank Open Data, 17 January 2019. *Age dependency ratio (% of working-age population): Japan and Zambia*.)

<sup>288</sup> United Nations Population Fund (UNFPA) website, 18 January 2019. *Population and poverty*.

<sup>289</sup> Larmer 2010, 50.

<sup>290</sup> World Population Review website, 23 January 2019. *Zambia Population 2019*.

<sup>291</sup> Ferguson 1999, 1–2.

<sup>292</sup> World Bank Open Data, 11 January 2019. *Urban population (% of total): Zambia*. It is important to note that because of the accelerating population growth, the number of urban residents continued to climb in absolute terms after 1980. In 2017 more than seven million people lived in urban areas, while in 1980 the figure was less than 2.5 million. (World Bank Open Data, 11 January 2019. *Urban population: Zambia*.)

was slashed, and practises such as street vending increased. In 1999, only 11 per cent of Zambians worked in formal employment.<sup>293</sup>

In some early Western studies the distinct cultures of Zambian urban classes were highlighted, but later research has proven that the experiences of rural and townspeople have not been so significantly different. Moreover, cyclical movement between towns and rural areas have distorted earlier data somewhat.<sup>294</sup> However, Miles Larmer emphasises the fact that “the perception that Zambia was a highly urbanized (or overurbanized) country (whatever the material reality) was important in shaping urban Zambians’ sense of identity”<sup>295</sup>.

Zambia’s postcolonial economic history is a tale of underdevelopment and unfulfilled potential. After five years of sovereign rule, Zambia was one of the richest countries in Africa. On a global scale, it was classified as a middle-income country, ranking ahead of the likes of Brazil, Malaysia, Turkey and South Korea when comparing GDP per capita.<sup>296</sup> Today, the average Zambian income lingers around 1 500 dollars a year, which is slightly lower than the median level of Sub-Saharan Africa.<sup>297</sup> On a global ranking it is in 154th place, behind Uzbekistan and ahead of Cameroon. For the sake of comparison, the average yearly incomes in Malaysia and Brazil are nearly 10 000 dollars, with Turkey slightly ahead of that mark. The rise of South Korea to become the biggest economy among the “Asian Tigers”<sup>298</sup> is, of course, one of the most impressive feats in recent history.<sup>299</sup> A comparison of GDPs does not, however, sufficiently capture the full impact of the decline in the living standards and widespread poverty that Zambia has faced. One striking piece of evidence is the dramatic fall in life expectancy, which was 50 at the time of independence, but dropped to 35 during the following forty years.<sup>300</sup>

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<sup>293</sup> Hansen 2008, 217.

<sup>294</sup> Larmer 2010, 50.

<sup>295</sup> Larmer 2010, 50.

<sup>296</sup> Ferguson 1999, 6.

<sup>297</sup> IMF Data Mapper, 11 January 2019. *GDP per capita, current prices: Zambia and Sub-Saharan Africa*.

<sup>298</sup> The term refers to the economies of South-Korea, Taiwan, Hong Kong and Singapore which grew at a remarkably fast pace from the 1960s to the 1990s. A World Bank report from 1993 attributed the rise of the tigers to neoliberal policies, but later studies have argued that state-led interventions and protective policies explain the growth in a more satisfactory way. For a detailed discussion, see Chang 2006.

<sup>299</sup> IMF Data Mapper, 11 January 2019. *GDP per capita, current prices: Brazil, Republic of Korea, Malaysia, Turkey and Zambia*.

<sup>300</sup> Gewald, Hinfelaar & Macola 2008, 3.

The history of large-scale copper extraction in Zambia has its roots in the 1890s. After “discovering” vast copper deposits in the region, Cecil Rhodes<sup>301</sup> and his British South Africa Company (BSAC) started securing mining rights from local rulers. The BSAC officially founded Northern Rhodesia in 1911 and thirteen years later it became a protectorate of the British Colonial Office.<sup>302</sup> The BSAC reserved the mining rights and massive constructions were started in the Copperbelt region. Larmer describes how “many people, mainly Africans, suffered terribly in the process, but they built one of the greatest concentrations of industry and urban development in the African continent”<sup>303</sup>.

The fortunes of the mining sector have defined Zambian economic development. Between 1964 and 2012, the mining industry generated a third of the gross national income (GNI)<sup>304</sup> on average.<sup>305</sup> While the importance of the copper industry has been enormous, the deterioration of it has been equally remarkable. The debt crisis practically stifled all new investments and the falling revenues from the nationalised mines were hoarded by the state. No new mines were established after 1979.<sup>306</sup> As investments plummeted the quality of the Zambian copper ore dropped 20 per cent throughout the 1970s.<sup>307</sup>

The stagnation is best reflected in the volumes of production. At its peak, copper production reached 750 000 tons in 1974, but by 2000 the national mining conglomerate, Zambia Consolidated Copper Mines (ZCCM), was extracting only 257 000 tons of copper a year.<sup>308</sup> Production picked up finally when rising copper demand in China and India kicked off a new boom in 2004. This was cut short by the global financial crisis of 2008, but copper prices recovered quickly after the crash. In 2017, a record of 850 000 tons of

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<sup>301</sup> Cecil John Rhodes (1853–1902) was a British businessman and politician who made his career in Southern Africa. He led the British South Africa Company (BSAC) and founded Rhodesia in 1895. His most prominent political assignment came in 1890, when he was chosen as the prime minister of the Cape Colony. The legacy of Rhodes is very controversial. After his death, his funds were used to establish the Rhodes scholarship, which offered students from around the globe the chance to study in the University of Oxford. Critical commentators have focused on Rhodes’ belief in the supremacy of the British race and Empire. The legacy has been further politicised in recent years with the emergence of a protest movement called Rhodes Must Fall. The movement – launched in South African universities – called for the abolition of Rhodes’ memorials and for a broader campaign to decolonise education. For a more detailed account on the contemporary discussion, see Newsinger 2016.

<sup>302</sup> Fraser 2010, 3–4.

<sup>303</sup> Fraser 2010, 4.

<sup>304</sup> GNI and GDP are frequently used as substitutable terms. Their main difference is that GNI takes into account the wealth that a country’s residents acquire abroad as well.

<sup>305</sup> Boos & Holm-Müller 2016, 882.

<sup>306</sup> Fraser 2010, 9.

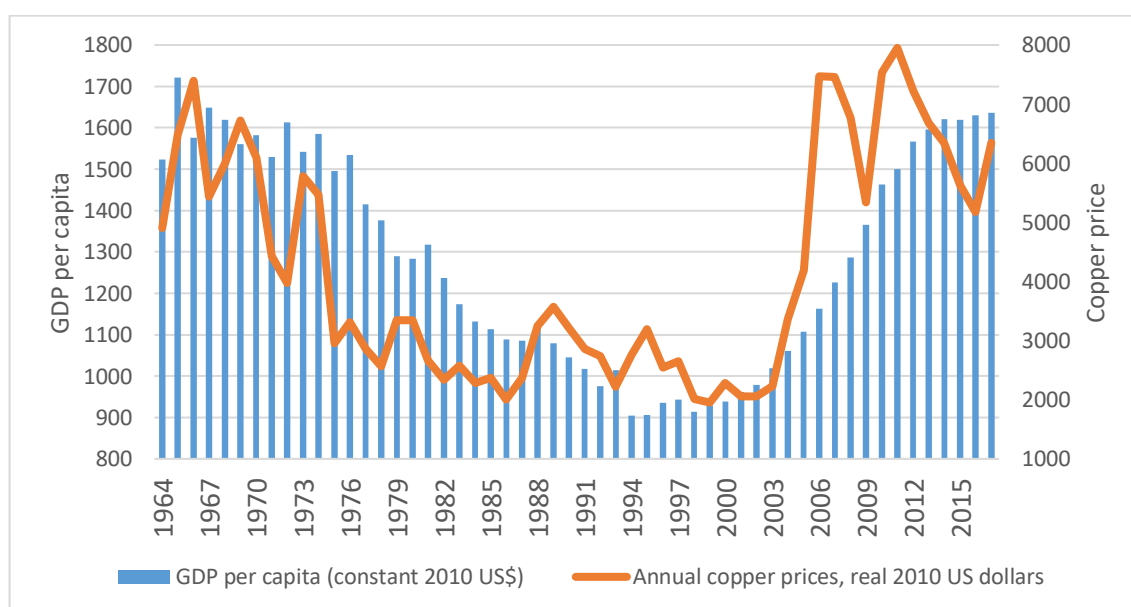
<sup>307</sup> Auty 1991, 178.

<sup>308</sup> Fraser 2010, 9.

copper was produced in Zambia.<sup>309</sup> The reliance on copper is captured strikingly when comparing the price fluctuations of the commodity with the trajectory of the GDP per capita of postcolonial Zambia (See Figure 2, page 61).

Why has a relatively peaceful and resource-rich country not been able to create wider prosperity for its people? This failure can be attributed to many factors. At first sight bad luck seems to be a crucial explanation, as Alistair Fraser shrewdly points out in the introductory chapter of the book *Zambia, Mining, and Neoliberalism: Boom and Bust on the Globalized Copperbelt*, which he has co-edited with Larmer. The first North Rhodesian copper mines started operating in 1929 just before the onset of the Great Depression, and the Zambian government's decision to nationalise the mines was shortly followed by the crash of global commodity prices in 1974. The misfortune continued to the new millennia as the Zambian government was pressured to privatise the unprofitable mines in 1997–2000. A lion's share of the revenues from the boom that started in 2004 was then collected by multinational mining companies.<sup>310</sup>

**Figure 2. GDP Per Capita and Annual Copper Prices: Zambia 1964–2017**



(Sources: World Bank Commodity Price Data. *The Pink Sheet*; World Bank Open Data. *GDP per capita (constant 2010 US\$): Zambia*.)

<sup>309</sup> Times of Zambia, 29 January 2018.

<sup>310</sup> Fraser 2010, 1–2.



Although horrific timing in relation to international copper prices has certainly contributed to Zambia's economic woes, it is not a sufficient explanation alone. While troubles in the Zambian mining industry have resulted in economic decline, the booms in the sector have not contributed significantly in disbursing national wealth to the larger population. Larmer sums this up in saying that "the historical evidence suggests that there has never been a direct or causal relationship between the fortunes of the mining industry on the one hand and the general prosperity of Zambia or Zambians on the other"<sup>311</sup>. Therefore, the volatile international copper markets are only part of the problem.

While a strong mining industry undoubtedly creates great export potential, an overreliance in one sector of the economy can be problematic. In the economic literature concerning Zambia one commonly encounters the term "Dutch disease". The term was coined by *The Economist* in 1977, when the newspaper analysed the economic situation of the Netherlands. At the time, the Dutch economy reaped great revenues by exporting natural gas, but this had adverse effects on other sectors of the national economy. The newspaper determined that the influx of foreign currency, caused by the booming exports, lead to an overvaluation of the Dutch guilder. This resulted in making other sectors of the economy less competitive and was followed by a plunge in investments and rising unemployment. In a fixed currency regime, as is the case with Zambia, the mechanism and results are only slightly different. The extra foreign currency is converted to the domestic equivalent causing an expansion in the supply of money. This in turn pushes prices up and is followed by the appreciation of the "real" exchange rate<sup>312</sup>. Once again, the end result is a drop in competitiveness and investments.<sup>313</sup>

As with most economic models, reality tends to be more complicated. Indeed, the Dutch disease does not work in a uniform way in varying settings. Nevertheless, the Dutch disease is a handy tool for analysing the difficulties faced by undiversified economies that are relying on international commodity markets for export revenues. In recent years the Russian economy has encountered problems of this sort.<sup>314</sup> While concentrating in the

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<sup>311</sup> Larmer 2010, 32.

<sup>312</sup> The real exchange rate measures the relative price levels of two countries with the help of consumption baskets and the nominal exchange rate. The nominal exchange rate indicates the relative price of two currencies.

<sup>313</sup> *The Economist*, 5 November 2014.

<sup>314</sup> Kalcheva & Oomes 2007.

production of one commodity is not inherently harmful, troubles will surely commence if commodity prices are volatile, as is the case with copper in Zambia and oil in Russia. Several studies have proven that the Dutch disease has plagued Zambian development ever since independence.<sup>315</sup> Moreover, Steve Kayizzi-Mugerwa's calculations imply, that while the Zambian economy has been hurt by the Dutch disease during mining booms, busts on the other hand, don't simply reverse the effects and make other sectors more competitive.<sup>316</sup>

As an economic model the Dutch disease has its limitations. Most importantly, it does not take into account the varying socio-political contexts of the commodity-exporting countries. The Dutch society differs crucially from, say, the Russian, Venezuelan or Zambian counterpart. In this light, a further possible Zambian predicament can be what researchers have named the "resource curse". The resource curse has been offered as an answer to the larger question of mineral-rich developing countries faring worse than states that have no natural resources. Zambia is often cited as the most clear-cut example of a state that has been plagued by it<sup>317</sup>.

Graham Davis presents a comprehensive critique of the sectoral analysis tradition that has tried to identify reasons behind poor development in mineral exporting economies since the early 1990s.<sup>318</sup> Numerous investigations have set out to specify possible factors that contribute to socio-political environments fostering development on one hand and impairing it on the other. Possible explanations vary greatly from cultural and religious traditions to different forms of structural determinism. Davis reckons that no general results behind the resource curse can be identified, and therefore a case-specific approach is more fruitful in studying the phenomenon.<sup>319</sup>

Davis' critique carries more profound assertions. As the often-cited example of South Korea proves, development economists tend to agree that a healthy portion of state control is needed for fostering sustainable growth. According to some explanations then, the curse is very real, as mineral extraction is believed to causally produce bureaucratic incapacity of the state.<sup>320</sup> Instinctively thinking, however, this seems quite implausible.

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<sup>315</sup> Meijer 1990; Kayizzi-Mugerwa 1991; Boos & Holm-Müller 2016.

<sup>316</sup> Kayizzi-Mugerwa 1991, 860.

<sup>317</sup> Boos & Holm-Müller 2016; Haber & Menaldo 2011.

<sup>318</sup> Davis 1998.

<sup>319</sup> Davis 1998, 218.

<sup>320</sup> Davis 1998, 221.

To take a contemporary case in point, it would be simplistic to blame oil for Venezuela's recent hardships. Rather, the extraction of oil has helped a corrupted and dictatorial state to legitimate and maintain its power. The extraction of oil has *enabled* state corruption, but by no means has it necessitated it. Thus, it would be more reasonable to deduce that mineral extraction combined with a weak state can result in a vicious circle that fosters corruption and hampers development.

Classical development economics highlights the importance of import substitution and export promotion in diversifying the national economy. In the studies conducted in the 1980s and 1990s, manufacturing was identified as the crucial sector to be promoted.<sup>321</sup> While this recipe certainly worked well in some Asian countries in the past, it sounds severely outdated in the rapidly changing global environment of today. Moreover, neoclassical economics suggests that diversification is not as all-powerful a solution as its proponents imply. According to one of the most famous paradigms, a country should focus on the production of commodities where it has a comparative advantage in relation to its trading partners.<sup>322</sup> Thus, in theory, even a Dutch-disease situation should actually be welcomed, because it diverts resources from other uncompetitive sectors to the booming minerals production.<sup>323</sup>

While the possibility of finding general and straightforward ways to deal with the resource curse is questionable, it is clear that developing countries relying on mineral exports do face problems of their own. Mineral extraction is not very labour intensive, so promoting other sectors of the economy is vital. Using Zambia as a case, R.M. Auty constructs a theoretical model, the corroding feedback loop, in which the effects of an external shock are compounded by a weak government that resorts to clientalistic rent-dispensing policies. Other parts of the loop include uncompetitive export sectors, an overvalued exchange rate, the accumulation of debt and widespread corruption.<sup>324</sup> Although I disagree with the general conclusions that Auty draws from the case, he is right in that features of this kind have affected Zambian development since the oil crisis.

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<sup>321</sup> Davis 1998, 219.

<sup>322</sup> The theory of comparative advantage was formulated in 1817 by David Ricardo in his book *On the Principles of Political Economy and Taxation*.

<sup>323</sup> Davis 1998, 223–224.

<sup>324</sup> Auty 1991, 171.

More recently, Adrian Boos and Karin Holm-Müller have applied an econometric approach in studying the relationship of mineral dependence and Genuine Savings (GS), an indicator coined by the World Bank, which measures the reinvestment of rents from the depletion of natural resources in human and physical capital.<sup>325</sup> Their findings indicate that Zambia has been affected by the resource curse, because “Zambian GS proved highly volatile and completely dependent on world copper prices and to a lesser extent on political developments”<sup>326</sup>. According to the study, in addition to external factors, two endogenous elements have contributed to the low reinvestment level in Zambia: a semi-authoritarian political system and weak institutions that foster corruption.<sup>327</sup> Widespread corruption at the very top level of government is a relatively recent phenomenon, however, because “only during the decade of Chiluba’s rule from 1991 onwards did corruption become entrenched and murkily intertwined with the political class”<sup>328</sup>. The most common form of corruption is often not financial but instead takes the form of patronage. Corruption has resulted in a bureaucratically large and wasteful public sector, which consumes a lot of the national budget and allocates mineral rents unproductively.<sup>329</sup>

To conclude, I follow Davis in maintaining that the resource curse – as a dilemma hampering all resource-rich and export-oriented countries – is a myth. A comparison of Chile and Zambia, both economies heavily reliant on copper exports, is sufficient in establishing this conclusion.<sup>330</sup> Moreover, Botswana, Zambia’s sparsely populated neighbour, has been very successful in managing to reinvest mineral rents in a sustainable way, with the state taking an active role in the process.<sup>331</sup> In 1985, nearly 60 percent of the Botswanan population lived in poverty, but in the following 25 years the number decreased to a third of that.<sup>332</sup> On the other hand, it is equally clear that a certain amount of diversification is needed because in a globalised economy an overreliance on one commodity is simply not sustainable. Mineral dependence is especially damaging when global prices are low or falling.<sup>333</sup> Thus, the failure to diversify the economy before and

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<sup>325</sup> Boos & Holm-Müller 2016, 882.

<sup>326</sup> Boos & Holm-Müller 2016, 911.

<sup>327</sup> Boos & Holm-Müller 2016, 904–911.

<sup>328</sup> Boos & Holm-Müller 2016, 908.

<sup>329</sup> Boos & Holm-Müller 2016, 908.

<sup>330</sup> Davis 1998, 226.

<sup>331</sup> Lange & Wright 2004.

<sup>332</sup> World Bank Open Data, 25 January 2019. *Poverty headcount ratio at national poverty lines (% of population): Botswana.*

<sup>333</sup> Davis 1998, 224.

during the long mining bust that lasted approximately three decades, is a key element in an understanding of Zambian development.

Both concepts – the Dutch disease, and the resource curse especially – have some serious shortcomings, but I believe that they nevertheless are useful tools in helping to understand why the Zambian economy has not been able to produce sustainable growth. The copper industry has damaged other sections of the economy and, even during the export booms, the spoils have not filtered down adequately to the poorest parts of society. This failure has been exacerbated by a weak and authoritarian state that has invested mineral rents inefficiently, in addition to being unable to take the decisive steps to diversify the economy. I have included the above discussion in the study, because I believe that it provides a useful theoretical framework which can be carried along with the historical analysis. The issue of diversification has been central to the Zambian economy and the question was recognised early in Zambian domestic politics and in the IFIs.

### **3.2 The Boom and Nationalisations: 1964–1973**

Miles Larmer highlights the fact that the battle to control the Zambian mining revenues has always been a political contest.<sup>334</sup> Due to the steadily increasing mining revenues in the 1950s, the question became acute as the struggle for independence intensified. After the formation of the short-lived Central African Federation (CAF)<sup>335</sup> in 1953, revenues from the mines in the Northern part of the federation were largely pocketed by Southern Rhodesia's white settlers.<sup>336</sup> Thus, "nationalist opposition to the Central African Federation in Northern Rhodesia was framed in terms of resistance to white settler control of the territory's mining resources"<sup>337</sup>. Furthermore, the process was guided by the understandable principle of directing mining revenues to the general development of the emerging state.

The Zambian struggle to control the means of production was by no means unique. On the contrary, it was a common experience for the decolonising states of the world at the

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<sup>334</sup> Larmer 2010, 32.

<sup>335</sup> The CAF (1953–1963) was a semi-autonomous federation that tied together the British colony of South Rhodesia (later Zimbabwe) and two British protectorates, Northern Rhodesia and Nyasaland (independent Malawi from 1964 onwards).

<sup>336</sup> Larmer 2010, 34.

<sup>337</sup> Larmer 2010, 43.

time: “new rulers had secured political power at independence but remained dependent for resources on unequal relationships with the governments and companies of the former colonial powers”<sup>338</sup>. In Zambia, the transition was relatively smooth as a thoroughly negotiated and mutually respected partnership was forged between the UNIP government and the two major mining companies, which held the mining rights in the Copperbelt: Anglo American Corporation (AAC) and Rhodes Selection Trust (RST).<sup>339</sup>

Although the so called First Republic (1964–1973) was ostensibly a multi-party democracy, the first years of Zambian independence were characterised by a steady decline of civil liberties and a waning tolerance of dissidents.<sup>340</sup> In fact, Larmer criticises earlier historiography for its “unproblematic” stance in relation to the First Republic. In these accounts, the initial steps of development are often seen as sufficient in satisfying the expectations of Zambians.<sup>341</sup> Indeed, authoritarianism was not born over-night in December 1972 when President Kaunda announced that Zambia was to become a “one-party participatory democracy”.<sup>342</sup> Giacomo Macola distinguishes the political undercurrents that planted the seeds of early authoritarianism.<sup>343</sup> Kaunda’s rise to ascendancy had not been inevitable, as he had to defeat a rival party, the African National Congress of Northern Rhodesia (ANC)<sup>344</sup>, and its charismatic leader Harry Mwaanga Nkumbula in the first general elections of 1964. The relations between the two parties and their leaders had turned sour in the preceding years and a ferocious struggle for power paved the way to the elections. To this battle the UNIP “leadership reacted by elaborating an intellectual equivalence between party and national membership”<sup>345</sup>. In the process, a culture of political violence became gradually legitimated as both parties suppressed opposition movements in their stronghold areas.<sup>346</sup> Macola concludes that:

“Ideological seeds of the one-party state and its natural corollaries, a much-heralded belief in the leader’s infallibility and a totalitarian ambition to quash and/or

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<sup>338</sup> Fraser 2010, 7.

<sup>339</sup> Larmer 2010, 35.

<sup>340</sup> Macola, 2008.

<sup>341</sup> Larmer 2008, 102.

<sup>342</sup> Larmer 2008, 98.

<sup>343</sup> Macola 2008, 17–44.

<sup>344</sup> After independence the party adopted the name Zambian African National Congress. Kaunda had initially been a member of the ANC, but he left in 1958 and splintered his own party out of it. In comparison to UNIP’s socialist state driven economic planning, the ANC propagated itself as the defender of the interests of private businesses and free individuals. The ANC was popular among rural people in the South, while UNIP’s traditional stronghold was the Copperbelt province. (Macola 2008, 20, 29.)

<sup>345</sup> Macola 2008, 23.

<sup>346</sup> Macola 2008, 38–39.

encapsulate autonomous social movements, were already firmly embedded in the Zambian political soil well before the formal declaration of independence in October 1964.”<sup>347</sup>

Another significant reason for the state’s increasing willingness to oppress its own citizens stemmed from perceived threats to national security. In the early years of independence Zambia was very much a “frontier state”, in that it stood out as a sovereign indigenous nation in a very unstable part of the world. Most of its neighbours were either engaged in emancipatory struggles against colonisers or experiencing civil unrest of some degree. Many of the conflicts were proxy wars with global superpowers taking sides in the familiar spirit of the Cold War.

For Zambia, the situation across its Southern border was most disturbing. In November 1965, Ian Smith, the leader of Rhodesia’s white settler minority, announced a Unilateral Declaration of Independence (UDI).<sup>348</sup> The Zambian government urged the UK to quash what it viewed as a rebellion, but only a small number of British troops were sent to the region. Prime Minister Harold Wilson (1964–1970, 1974–1976) opted instead to use UN-imposed economic sanctions to tie down Rhodesia.<sup>349</sup> The persistent conflicts in neighbouring states, and the planned production of nuclear weapons by South Africa, the region’s biggest threat to Zambian existence, gave rise to precarious feelings in regard to national security.<sup>350</sup> This undoubtedly amplified the UNIP government’s eagerness to tighten its grip domestically.

The geopolitical tensions had significant impacts on economic considerations as well. In the first few years of independence, Zambia was wholly reliant on Rhodesia when it came to importing oil and exporting copper. The falling-out with Rhodesia and subsequent sanctions meant that the Zambian government had to look for other options in securing the supply of energy and in the continuation of trade. Fortunately, the US was dependent on Zambian copper at the time. For that reason, the government of Lyndon B. Johnson (1963–1969), together with the British government, organised a temporary air lift, which brought in the oil to run the mines in the Copperbelt. When the conflict with Rhodesia

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<sup>347</sup> Macola 2008, 24–25.

<sup>348</sup> None of the world’s independent states recognised the UDI. Despite this, Rhodesia’s minority government managed to hold on to power for nearly 15 years with the help of South Africa and Portugal. After a long guerrilla war, independent Zimbabwe emerged in 1980. The first elections were won by Robert Mugabe (1924–), who stayed in power for 37 years.

<sup>349</sup> DeRoche 2008, 79–81.

<sup>350</sup> DeRoche 2008, 88.

became prolonged, Zambia found an ally in Tanzania. An oil pipeline connecting the two states was built by an Italian company in 1968. Another vital piece of infrastructure was the planned new railway line that would connect the Zambian mines to the port of Dar es Salaam in Tanzania. Funds were secured from a rather surprising source – the People’s Republic of China – after the British, American and Soviet governments had refused to finance the scheme. The construction began in 1970 and the TAZARA-railroad, spanning 1 860 kilometres, was completed five years later.<sup>351</sup>

Although Zambia was led by a socialist party, it did not align itself to the communist bloc. The Zambian government found most international sympathy in the so-called Non-Aligned Movement (NAM).<sup>352</sup> Most of the countries in the non-aligned movement promoted a program of state planning and economic nationalism. This was also the core of UNIPs economic strategy. Thus, although the relationship with foreign mining companies remained relatively good, a nationalisation of the Copperbelt mines was on the agenda soon after independence.

The urge to nationalise originated to a large extent from domestic politics although Rhodesia’s UDI and other international issues had a part to play as well.<sup>353</sup> According to Larmer, “in much of the country, local party officials were besieged by angry complainants bemoaning the lack of real development in their villages”<sup>354</sup>. On the other

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<sup>351</sup> DeRoche 2008, 82–89.

<sup>352</sup> NAM was established in 1961 by the leaders of Yugoslavia, India, Egypt, Indonesia and Ghana. The purpose of the movement was to resist the bloc-politics of the Cold War environment. NAM quickly gained widespread support, especially among newly independent ex-colonies. While a plethora of different ideologies were represented among the member states, common goals included the denouncing of imperialism and a commitment to work for world peace. In 1970, Zambia hosted the third NAM summit in Lusaka.

<sup>353</sup> The nationalisations should be viewed against the backdrop of growing frustrations in the international context. The countries of the global South had promoted for a New International Economic Order (NIEO) in the UN, which sought to change the underlying economic dynamics of the world that still very much followed the extractive patterns of colonial times. While the NIEO received a lot of support and sympathy – even from Western countries – the established world powers were able to preserve their hegemony in the system. Moreover, President Kaunda worked actively through the NAM in order to organise a cartel of copper producing countries that would resemble the Organisation of Petroleum Exporting Countries (OPEC). Kaunda felt that the copper producing countries were in an unfair position, because they had no way of influencing the price fluctuations of the commodity. In 1967, the Intergovernmental Council of Copper Exporting Countries (CIPEC) was established in Zambia. Other founding members included Chile, Peru and Congo. Although a few other copper producing states joined later, the CIPEC never became a price- and quota-fixing cartel as such, and turned out to be a rather unimportant consultative body instead. (Fraser 2010, 6–7.)

<sup>354</sup> Larmer 2010, 36.



hand, most of the mineworkers in the Copperbelt were Bemba-speaking<sup>355</sup> UNIP supporters who had played a major role in the nationalist struggle. This constituency, led by Kaunda's increasingly radical party comrade, Simon Kapwepwe (1922–1980), demanded more returns from its representatives as well. Under piling pressure from many fronts, Kaunda decided to nationalise the mines.<sup>356</sup> Thus, it can be reasoned that ethnic tensions and a culture of patronage shaped Zambian postcolonial politics from the very beginning.

The nationalisations were a key component of the Mulungushi Economic Reforms of 1968. In the next year, the state claimed a 51 per cent stake in the two big mining corporation's operations in Zambia and formed two parastatal companies, Nchanga Consolidated Copper Mines (NCCM) and Roan Consolidated Mines (RCM).<sup>357</sup> The nationalisations were wide-ranging, as an equally large share was acquired in other major foreign-owned industrial and financial firms. The process of nationalisation progressed gradually, so that by 1975, the Zambian state had taken full control of the mines and other vital assets.<sup>358</sup>

Besides taking control over foreign firms, economic nationalism was displayed in the reform package more generally. Hugh Macmillan has investigated the impact of a set of laws that were introduced in order to encourage indigenous trading and retailing.<sup>359</sup> At the time, Zambian trade and retail was dominated by a few big foreign companies and, especially in the countryside, by entrepreneurs of Indian origin. The novel laws pressured bigger firms to "voluntarily" offer majority stakes of their companies to the state, and restricted "resident expatriate businesses" (mainly Indians in this case) to running their enterprises in the centres of ten large towns.<sup>360</sup> While a Fund-report in 1973 cited Zambian representatives saying "that the transition has caused very little, if any, disruption"<sup>361</sup>, the truth was quite the opposite. Macmillan emphasises the long-term consequences of the

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<sup>355</sup> The Bemba people are the largest ethnical group in Zambia comprising approximately 20 per cent of the population. In addition to being spoken by the Bemba people, the Bemba language is the lingua franca of 18 different ethnic groups, some of which live in neighbouring Congo, Botswana and Tanzania.

<sup>356</sup> Larmer 2010, 36.

<sup>357</sup> In 1982, NCCM and RCM were merged together to form one giant national mining company, Zambia Consolidated Copper Mines (ZCCM). (Larmer 2010, 41.)

<sup>358</sup> McPherson 2004a, 41.

<sup>359</sup> Macmillan 2008.

<sup>360</sup> Macmillan 2008, 190–191.

<sup>361</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1972 ARTICLE XIV CONSULTATION, 6. *SM/73/31*, 2/14/1973.

reforms. The long depression that kicked in after the copper price shock of 1975 was more severe in the countryside, because traditional trading networks had been broken up and new businesses failed to replace them. This – coupled with newly introduced price controls – hampered agricultural output particularly, as farmers lost the incentive to produce for local markets.<sup>362</sup> Macmillan reckons that the Mulungushi economic reforms did not cause the later depression, but they certainly made it longer and more damaging.<sup>363</sup>

Agriculture was singled out as a vital sector for the development of the Zambian economy already in the first national economic program in 1966. The rhetoric did not, however, materialise in reality. While government spending rose significantly in the years from 1966 to 1970, the same cannot be said of inputs to agriculture.<sup>364</sup> Malcom F. McPherson determines the main reasons behind the persistent lack of development that continued in the following decades. They include state-influenced low producer prices (the low cost of food was directed to please urban workers), an overvalued exchange rate plus a lack of investment in production boosting activities and infrastructure.<sup>365</sup> The UNIP government encouraged the formation of farming cooperatives but they proved to be unproductive.<sup>366</sup>

Life in the booming Copperbelt during the 1960s was an exciting time. Mining revenues and generous subsidies created wealth and a buzzing urban atmosphere with “an unusually high concentration of motor cars, fashionable hairstyles, and European-style nightclubs”<sup>367</sup>. Strong trade unions were formed in the Copperbelt already in the 1950s and they had played an important part in the nationalist struggle.<sup>368</sup> After independence, the alliance with UNIP became strained, because the state recognised that wage growth had to be controlled. The unions responded with strikes and the question was tied to the differences of income between African and expatriate workers.<sup>369</sup> As a result, the UNIP-government and the foreign mining companies had to submit to pay rises. The Fund estimated that Zambian wages grew 22 per cent annually between 1965 and 1968, before

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<sup>362</sup> Macmillan 2008, 210.

<sup>363</sup> Macmillan 2008, 212.

<sup>364</sup> McPherson 2004b, 295–296.

<sup>365</sup> McPherson 2004b, 296, 306.

<sup>366</sup> Auty 1991, 173.

<sup>367</sup> Fraser 2010, 8.

<sup>368</sup> Fraser 2010, 5.

<sup>369</sup> Larmer 2010, 43; McPherson 2004a, 39–40.

a wage freeze was implemented by the government in 1969.<sup>370</sup> The strong leverage of the mine workers was one reason that made the nationalisations more appealing to Kaunda as they “aimed to increase both the effective control of strategic mineral resources and the human resources vital to their exploitation”<sup>371</sup>.

The years after independence witnessed an expansion of the public sector. Worryingly, the civil service proved useful for the government in rewarding loyalty as sinecures became common.<sup>372</sup> Contrary to the recommendations of the first economic plan, the UNIP leadership pushed for growth in both wages and employment. As a result the government wage bill reached quickly to a sizable ten per cent share of the GDP.<sup>373</sup> According to Boos and Holm-Müller, the creation of a “large and inefficient bureaucratic apparatus” is a customary feature in resource-rich countries that are shaped by patronage.<sup>374</sup> The heavy public sector aggravated the failed efforts to promote agriculture and diversify the economy. To conclude, the economic policies during the First Republic did not encourage diversification and, in fact, they strengthened the bias towards the urban working class at the expense of the rural poor. Auty sums up the consequences: “the overall effect of post-independence policies was to deploy high rents from copper primarily to expand and reinforce a powerful urban rent seeking constituency whose income from mines, factories and offices outstripped productivity”<sup>375</sup>.

The Bank had funded a few projects already under the British rule in Northern Rhodesia. By far the biggest project before independence was the Kariba power dam, built on the Zambezi-river bordering Northern and Southern Rhodesia. The Bank loaned 80 million dollars to the project, and the bill was split in half between the two territories.<sup>376</sup> After independence the rate of new projects grew significantly, as altogether 14 new projects were undertaken between 1966 and 1974.<sup>377</sup> Financially the weightiest projects were still in infrastructure. Two highway projects were initiated in 1966 and 1968 respectively.<sup>378</sup>

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<sup>370</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1970 ARTICLE XIV CONSULTATION, 6. SM/71/8, 1/19/1971. IMF Archives.

<sup>371</sup> Larmer 2010, 45.

<sup>372</sup> Boos & Holm-Müller 2016, 905.

<sup>373</sup> McPherson 2004a, 40.

<sup>374</sup> Boos & Holm-Müller 2016, 905.

<sup>375</sup> Auty 1991, 174.

<sup>376</sup> World Bank 1958, ii. *Rhodesia and Nyasaland – Economic position and prospects (English)*. World Bank Archives.

<sup>377</sup> World Bank website, 8 February 2019. *Where We Work / Zambia / All Projects*.

<sup>378</sup> The first highway loan (17.5 million dollars) was the first Zambian loan financed by the IDA. The need to reconstruct parts of the highways stemmed from Rhodesia’s UDI, which redirected traffic to the roads

In the next decade, the Bank agreed to provide a total of 82.1 million dollars to build another power station at the Kariba-site. In 1973, a similar power project at the Kafue-river was funded with a substantial loan amounting to 115 million dollars.<sup>379</sup>

Following the Bank's intellectual reorientation, a gradual shift in the emphasis of the projects can be detected through the early years of Zambian independence. In 1968, the Bank's first ever forestry project was initiated in Zambia. The scheme was considered a success in a later project performance report.<sup>380</sup> On the other hand, a loan for a livestock development project was cancelled by the Zambian government after the parastatal company in charge of implementation got into financial trouble.<sup>381</sup> By 1973, the Bank had also made a commitment to invest significantly into Zambian education. In the following years the Bank disbursed over 50 million dollars to three projects that were directed to improve secondary education, teacher training, vocational schooling and the standard of universities. The projects yielded somewhat positive, but overall mixed results.<sup>382</sup> The clearest sign of the Bank's new agenda can be seen in a 20 million project in 1974, which was designed to improve the living standards of urban squatters in Lusaka.<sup>383</sup>

The Zambian authorities interacted quite frequently with Fund-officials through the 1960s, but since the macroeconomic situation of the country remained largely good, the relationship was more or less consultative. Overall, people at the Fund seemed pleased with developments in Zambia. In a meeting held in February 1968, the executive directors noted the fine performance of the Zambian economy despite the complications brought about by Rhodesia's UDI, although increasing government expenditures were seen as slightly alarming.<sup>384</sup> A staff report next year was mainly optimistic, but it did raise

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from the Rhodesia Railways. (World Bank 1966, 2-3. *Zambia – Highway Reconstruction Project (English)*. World Bank Archives).

<sup>379</sup> In the Bank's later assessment both projects were deemed financially disappointing, because political tensions between Zambia and Rhodesia affected the two joint power ventures. In addition, power demand turned to be a lot smaller in Zambia and Zimbabwe in the 1980s than calculations a decade earlier had predicted. To gauge the size of the loans it is helpful to notice that the entire GDP of Zambia was 2.27 billion dollars in 1973. (World Bank 1983a, 37–38. *Zambia – Kariba North Hydroelectric Project (English)*; World Bank 1985a, iv–v. *Zambia – Kafue Hydroelectric Project – Stage Two (English)*. World Bank Archives; World Bank Open Data, 27 March 2019. *GDP (current US\$): Zambia*.)

<sup>380</sup> World Bank 1977. *Zambia – Industrial Forestry Project (English)*. World Bank Archives.

<sup>381</sup> World Bank 1976a. *Zambia – Livestock Development Project (English)*. World Bank Archives.

<sup>382</sup> World Bank 1983b, 11–13. *Zambia – First and Second Education Projects (English)*; World Bank 1985b, 30–31. *Zambia – Third Education Project (English)*. World Bank Archives

<sup>383</sup> World Bank 1974. *Zambia – Lusaka Squatter Upgrading and Site and Services Project (English)*. World Bank Archives.

<sup>384</sup> EBM/68/18 – FEBRUARY 9, 1968, 18. *EBM/68/18, 2/9/1968*. IMF Archives.

concerns of stagnating agricultural production and the broadening gap between urban and rural incomes.<sup>385</sup>

Already in 1969, the Fund's staff appraisal had acknowledged that "the Zambian authorities are keenly aware and concerned over the vulnerability of the economy to a possible future fall in world copper prices"<sup>386</sup>. A report conducted a year later was more anxious. The Fund's staff were worried about a sharp fall in the global copper prices in 1970, as the commodity was accounting for 45 per cent of the Zambian GDP and 93 per cent of export earnings despite the efforts to diversify the economy. The volume of copper production tumbled as well, principally due to a severe flooding accident at the Mufulira mine, which had produced 25 percent of the total Zambian copper output.<sup>387</sup>

Although the report noted that agriculture was to take a centre stage in the government's next five-year economic plan, the sector was clearly in trouble according to it. Many expatriate commercial farmers had left the country and the government-organised cooperatives had largely failed.<sup>388</sup> Interestingly, the report concluded that the "Zambianisation" of the economy "has caused considerable dislocations, which the authorities believe to be of a transient nature"<sup>389</sup>. While implying the harmfulness of these policies and recommending some repairing actions, the Fund was not yet in a position to dictate Zambian economic policy and the critique was confined to the level of rhetoric.

The economic downturn forced Zambia to seek financial help from the Fund for the first time in December 1971. The Fund agreed to the Zambian authorities' acquisition of 19 million dollars from the Compensatory Fund Facility (CFF), which was designed to assist in acute troubles following a decline in exports. The staff at the Fund believed that the shortfall in the export earnings was "largely attributed to circumstances beyond the control of the member"<sup>390</sup>. In August 1972, Zambia borrowed another 19 million from the CFF. The Fund deemed the Zambian export shortfalls to fall into the category of being

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<sup>385</sup> ZAMBIA – 1969 ARTICLE XIV CONSULTATION, 1-2. *SM/69/168*, 11/18/1969. IMF Archives.

<sup>386</sup> ZAMBIA – 1969 ARTICLE XIV CONSULTATION, 13. *SM/69/168*, 11/18/1969. IMF Archives.

<sup>387</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1970 ARTICLE XIV CONSULTATION, 3. *SM/71/8*, 1/19/1971. IMF Archives.

<sup>388</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1970 ARTICLE XIV CONSULTATION, 5–6. *SM/71/8*, 1/19/1971. IMF Archives.

<sup>389</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1970 ARTICLE XIV CONSULTATION, 16. *SM/71/8*, 1/19/1971. IMF Archives.

<sup>390</sup> ZAMBIA – USE OF FUND RESOURCES, 4. *EBS/71/327*, 12/6/1971. IMF Archives.

caused by “disasters or major emergencies”, so that a rule limiting a member to 25 per cent of its quota in a 12-month period could be circumvented.<sup>391</sup>

Due to the difficulties in the copper industry, Zambian GDP contracted by four and eight per cent in 1970 and 1971, respectively. As the mechanism of the Dutch disease would indicate, other sectors of the economy grew in comparison, but not significantly enough to balance the loss in exports.<sup>392</sup> The border between Zambia and Rhodesia was closed permanently in January 1973. This damaged trade, because the TAZARA-railway was still under construction and about half of Zambian exports and imports still travelled through Rhodesia.<sup>393</sup> The good macroeconomic balance that Zambia had maintained since independence was in danger, as domestic credit expanded and foreign reserves decreased. The UNIP government responded by taking a more interventionist role in issuing price controls and restrictions on imports and capital transactions. The government continued its efforts to cut spending and to balance the budget. The budget deficits were financed mainly through credit from domestic banks.<sup>394</sup>

By March 1973 it was clear that additional external assistance was required. The Zambian government applied for a one-year stand-by arrangement (SBA) from the Fund, in which it would have the right to take out 19 million in Special Drawing Right (SDR)<sup>395</sup>, a quarter of the Zambian quota. The Fund staff approved the request as they assessed that “the Zambian authorities are making a reasonable effort to cope with the adverse impact of the border closure, and to improve the country’s financial position”<sup>396</sup>. While no specific policy conditions were outlined in the Fund’s decision, Zambian authorities were ordered to remain in close consultation with the Fund and a three-year deadline to repayment was set.<sup>397</sup>

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<sup>391</sup> ZAMBIA – USE OF FUND RESOURCES, 2. *EBS/72/210*, 7/3/1972. IMF Archives.

<sup>392</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1972 ARTICLE XIV CONSULTATION, 1-2. *SM/73/31*, 2/14/1973. IMF Archives.

<sup>393</sup> ZAMBIA – REQUEST FOR A STAND-BY ARRANGEMENT, 3. *EBS/73/134*, 4/24/1973. IMF Archives.

<sup>394</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1972 ARTICLE XIV CONSULTATION, 7-11. *SM/73/31*, 2/14/1973. IMF Archives.

<sup>395</sup> The SDR is the Fund’s supplementary reserve asset, created in 1969. The value of the SDR was originally measured in relation to gold and equalled the value of the US dollar. Since the collapse of the Bretton Woods system it has been determined by a currency basket. (IMF website, 13 February 2019. *Special Drawing Right (SDR)*.)

<sup>396</sup> ZAMBIA – REQUEST FOR A STAND-BY ARRANGEMENT, 10. *EBS/73/134*, 4/24/1973. IMF Archives.

<sup>397</sup> ZAMBIA – REQUEST FOR A STAND-BY ARRANGEMENT, 11-12. *EBS/73/134*, 4/24/1973. IMF Archives.

In December 1972, the era of one-party rule began in Zambia. A fierce internal battle in the UNIP had resulted in Kaunda's main rival, Simon Kapwepwe, forming his own party – the United Progressive Party (UPP) – in August 1971. Although ethnic tensions played a part in the birth of the party, the UPP was a heterogeneous political group that was unified by a feeling of injustice. Kapwepwe could claim a broad backing, as he enjoyed support among radical students and businesspeople in Lusaka alike. The president's response was swift and decisive. Kaunda banned all political parties (except his own) in February 1972 and sent 123 leading UPP members to jail. The constitution was amended to facilitate the one-party state and was adopted the next year. In his writings, Kaunda justified the one-party system by its compatibility with what he saw as authentic African tribal culture, which emphasises the importance of chiefly authority on the one hand, but communitarian decision making on the other.<sup>398</sup>

As he was consolidating his power, Kaunda unveiled the ambitious second national development plan (1972–1976). Agricultural self-sufficiency was a key element of the plan, with the government taking an active role in pricing, as well as subsidising seeds and fertilizers. Other major targets were a 36 per cent GDP growth and 100 000 new jobs in the five-year time frame. The plan consisted of massive investments, financed mainly by projected copper revenues and foreign and domestic debt. In total, the sum of capital expenditures in the plan reached two billion kwachas (approximately 3.12 billion dollars at the time).<sup>399</sup>

Owing to the hardships of the past couple of years, the government had to scale down the plan's investments substantially. In light of this, the Zambian government requested a 30-million-dollar program loan from the Bank to help finance the plan. After reviewing the plan, President McNamara gave the loan his full support.<sup>400</sup> The program loan was directed to finance vital imports in the short term, and the only condition was a provision that changes in the investment plan that affected the loan program would trigger a suspension. McNamara highlighted the need to implement some economic policies that the government representatives had proposed to a Bank mission in regard to achieving development over a longer time frame. The policy suggestions included a freeze of public

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<sup>398</sup> Larmer 2008, 98–106.

<sup>399</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1972 ARTICLE XIV CONSULTATION, 2–5. *SM/73/31*, 2/14/1973. IMF Archives.

<sup>400</sup> World Bank 1973a, 18. *Zambia – Program Loan Project (English)*. World Bank Archives

wages, cutting government subsidies, changes in pricing policies and a long-term view in planning external borrowing.<sup>401</sup> However, the loan was cancelled already in May 1974, because of the fast recovery in copper prices in 1973–1974. The remaining disbursements of the loan were diverted to the Kafue power station project instead.

The most intriguing Bank-document from this period dates back to May 1973, when a meeting of the executive directors was held to discuss the third education loan to Zambia. One of the directors raised concern over the growing indebtedness of Zambia and the significant amounts the Bank was investing in the country considering its small size.<sup>402</sup> McNamara acknowledged the apprehensions, and Senior Vice-President J. Bruce Knapp admitted that lending at the current level was not sustainable for a longer period.<sup>403</sup> Nevertheless, the Bank decided to go ahead with the loan. The captivating discussion exposes a few fundamental aspects of the Bank's position in relation to Zambia at the time. First and foremost, it reveals the Bank's conviction in that Zambia's predicaments were of a temporary character. While the volatility of copper prices was recognised, nobody – quite understandably – was anticipating the prolonged slump in commodity prices that was about to begin. Secondly, at this point in time, the Bank's senior staff clearly had trust in the UNIP government's ability to plan and implement sound economic policies.

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<sup>401</sup> World Bank 1973a, 15–17. *Zambia – Program Loan Project (English)*. World Bank Archives.

<sup>402</sup> World Bank 1973b, 7–8. *Transcript of meeting of the Executive Directors of the IBRD and IDA, held on Tuesday, May 31, 1973: Zambia – Third Education loan (English)*. World Bank Archives.

<sup>403</sup> World Bank 1973b, 8–11. *Transcript of meeting of the Executive Directors of the IBRD and IDA, held on Tuesday, May 31, 1973: Zambia – Third Education loan (English)*. World Bank Archives.



### 3.3 The Bust and Accumulation of Debt: 1974–1979

In hindsight, the short-lived rise in copper prices starting from January 1973 and subsequent momentary economic recovery was an adverse occurrence for Zambia. It reinforced the belief that copper price movements are cyclical. Thus, the response after the price shock in May 1974 was erroneous. When it would have been an appropriate time to start adjusting the economy, the UNIP government decided to finance its way out of troubles instead.<sup>404</sup>

If one wants to locate a turning point in Zambian postcolonial history, it can be pinpointed to April 1974. At the time, the price of copper reached 1.37 dollars per pound, a record figure. This was followed by a sharp plunge in May, and by December, the average price had fallen to 0.59 dollars per pound.<sup>405</sup> In the space of just a couple of months the copper price fell by more than 60 per cent.<sup>406</sup> Although the copper price shock was undoubtedly the biggest blow to the Zambian economy, it was compounded by the persistent problems in establishing secure trade routes, which in turn hiked up the costs of exports and imports. The TAZARA-railroad was completed in 1975, but its positive effects were largely outdone by a civil war erupting in neighbouring Angola. Due to the conflict, exporting copper through the port of Lobito on the Atlantic coast was no longer an option.<sup>407</sup>

The price shock had an immediate effect on the macroeconomic situation in Zambia. In just one year from 1974 to 1975, a swing worth 55 per cent of the entire GDP was recorded in the combined budget and balance of payments deficits.<sup>408</sup> The UNIP government did not blame external forces only. The Zambian authorities acknowledged that the projected rises in copper production in the second national development plan had been overestimated, and that the deep-seated problems constraining the agricultural sector had been underrated.<sup>409</sup> However, this frankness did not significantly alter the policies and priorities of the government. While the rate of investments and savings fell, public and private consumption continued at a high level.<sup>410</sup> The government levied higher costs

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<sup>404</sup> McPherson 2004a, 30.

<sup>405</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1974 ARTICLE XIV CONSULTATION, 3–5. *SM/75/91*, 4/18/1975. IMF Archives.

<sup>406</sup> Boos & Holm-Müller 2016, 895.

<sup>407</sup> Larmer 2010, 39.

<sup>408</sup> McPherson 2004a, 40–41.

<sup>409</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1974 ARTICLE XIV CONSULTATION, 7–8. *SM/75/91*, 4/18/1975. IMF Archives.

<sup>410</sup> McPherson 2004a, 33.

to foreign currency transactions ending a fairly liberal regime adopted since independence. The tougher controls, combined with an increasingly interventionist government, hindered economic activity, fuelled uncertainty and resulted in capital fleeing the country.<sup>411</sup>

The latter part of the 1970s was a time of stagnation in Zambia. A long recession hit the country hard and was accompanied with rapid accumulation of debt as the government opted to use external funds to finance large budget deficits. Credit was also used to sustain an outsized public sector and to finance food imports. As the viscous circle of increasing indebtedness gathered pace, new loans were increasingly used to repay earlier debt as well.<sup>412</sup> Initially, getting cheap credit was easy. According to Fernando R. Fernholz, “international financial agencies, flush with bank deposits from oil exporters, were eager to lend. They viewed the Zambian economy as basically sound with export earnings expected to recover”<sup>413</sup>.

During the last years of the decade, obtaining capital from the international markets became harder for Zambia. The response from the UNIP government was to draw credit from the Bank of Zambia, which in practise meant printing more money. This policy – common at the time in many parts of Africa and Latin America – has damaging effects for an economy in recession, not least by the inflationary pressure it creates.<sup>414</sup> In the five years from 1975 to 1980, the total sum of debt more than doubled from 1.6 billion dollars to 3.3 billion. At the turn of the decade the level of debt was already unsustainable, two years prior to the global debt crisis.<sup>415</sup>

Although the copper price shock received most of the attention, other problems in the Zambian economy were discussed in the Fund as well. In a document from November 1975, the staff at the Fund highlighted some of the UNIP government’s policies that they believed to have contributed to the financial distress. The policies included state subsidies on basic consumer goods that kept consumption at a high level and low producer prices that hampered growth in the agricultural sector.<sup>416</sup> The Fund approved Zambia’s request for new resources, but emphasised the need to diversify the economy and correct the

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<sup>411</sup> McPherson 2004a, 38, 43.

<sup>412</sup> Fernholz 2004, 265.

<sup>413</sup> Fernholz 2004, 265.

<sup>414</sup> McPherson 2004a, 38.

<sup>415</sup> Fernholz 2004, 266.

<sup>416</sup> ZAMBIA – USE OF FUND RESOURCES, 6. *EBS/75/413*, 11/18/1975. IMF Archives.

subsidies and pricing policies.<sup>417</sup> The only conditions in the loans denied the Zambian authorities the right to impose new levies or other restrictions on international capital transactions without consulting the Fund first.<sup>418</sup>

In July 1976, the Zambian authorities requested for a SBA equivalent of 62 million SDR. This time around the Fund-staff was considerably more straightforward about the UNIP government's mistakes. A report stated that "inappropriate demand management and pricing policies have caused a steady deterioration in the balance of payments position"<sup>419</sup>. The poor performance of the agricultural sector was once again highlighted as the report noted, that "since the independence of Zambia agricultural exports have virtually disappeared and food imports have increased"<sup>420</sup>. The Zambian authorities had drawn up a financial program to tackle the problems. In addition to fixing the above-mentioned deficiencies, the plan contained an exchange rate adjustment. Fund-officials recognised the overvaluation of the kwacha and agreed on the proposed 20 per cent devaluation of the currency.<sup>421</sup> Some conditions were attached to the SBA:

"The proposed stand by-agreement includes the following performance criteria: (a) a phased ceiling on the net domestic assets of the banking system, with a subceiling on net credit to government; (b) a phased reduction of payments arrears; and (c) the clause relating to exchange and import restrictions."

The criteria were outlined quantitatively in a table attached to the report. They aimed at restricting government borrowing from the banking system, curbing the escalating amount of debt and liberalising capital transactions. The SBA of 1976 was a prototype of later SAPs. It had a few conditions, but for the Fund staff at the time, it was sufficient that the Zambian authorities drew up a program consistent with Fund-recommended austerity measures. However, the SBA was cancelled shortly after adopting it, because Zambia failed to meet the conditions set by the Fund. Fresh monetary data revealed that the sub-ceiling on net credit to government had been surpassed, and in addition, the payments arrears continued to accumulate instead of gradually being phased out. Only 8.5 million

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<sup>417</sup> ZAMBIA – USE OF FUND RESOURCES, 12-13. *EBS/75/413*, 11/18/1975. IMF Archives.

<sup>418</sup> ZAMBIA – PURCHASE UNDER THE OIL FACILITY, 1. *EBS/75/412*, 11/18/1975. IMF Archives.

<sup>419</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 2. *EBS/76/307*, 7/12/1976. IMF Archives.

<sup>420</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 13. *EBS/76/307*, 7/12/1976. IMF Archives.

<sup>421</sup> ZAMBIA – EXCHANGE SYSTEM. *EBS/76/308*, 7/12/1976. IMF Archives.

SDR of the projected 62 million had been disbursed to Zambia at the point of cancellation.<sup>422</sup>

A staff report in January 1977 concluded that “the key policy choice to be made by the authorities now relates to the speed at which the existing internal and external imbalances should be corrected”<sup>423</sup>. The speed proved to be non-existent as economic woes deepened. In 1977, the real GDP of Zambia contracted and inflation climbed to 20 per cent. After a short-lived improvement, the balance of payments position deteriorated again in 1977 depleting Zambia’s foreign exchange reserves and accumulating external payments arrears alarmingly.<sup>424</sup> The mining companies were in increasing distress as copper prices did not recover and production lagged. In March 1978, a further 10 per cent devaluation of the kwacha was agreed with the Fund in order to boost the competitiveness of the sector.<sup>425</sup>

The exchange rate adjustment was once again tied to a larger stabilisation program which the Zambian authorities submitted to the Fund. The proposal consisted of familiar elements: a reduction in state subsidies, a wage freeze to cut expenditures and a push to diversify the economy by boosting agricultural production. The novel addition was the emphasis on the mining companies and their profitability.<sup>426</sup> A significant two-year SBA – totalling 250 million SDR – was negotiated in April 1978 to support the Zambian authorities’ effort to steady the ship. In addition to the SBA, Zambia purchased 48.75 million SDR from the CFF and 16 million SDR from the recently established Trust Fund.<sup>427</sup>

While backing the stabilisation program, the Fund was evidently increasingly critical of the UNIP government’s handling of the crisis. A report criticised the governments’ policies and failures to diversify the economy, stating that “virtually none of the

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<sup>422</sup> ZAMBIA – USE OF FUND RESOURCES – COMPENSATORY FINANCING, 4. *EBS/77/84*, 3/28/1977. IMF Archives.

<sup>423</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1976 ARTICLE XIV CONSULTATION, 16. *SM/77/16*, 1/17/1977. IMF Archives.

<sup>424</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1977 ARTICLE XIV CONSULTATION, 2. *SM/78/107*, 4/18/1978. IMF Archives.

<sup>425</sup> ZAMBIA – EXCHANGE SYSTEM. *EBS/78/144*, 3/17/1978. IMF Archives.

<sup>426</sup> Statement by Mr. Mogae on Zambia, 2–3. *BUFF/78/49*, 4/25/1978. IMF Archives.

<sup>427</sup> ZAMBIA – USE OF FUND RESOURCES – COMPENSATORY FINANCING, 13–14. *EBS/78/189*, 4/21/1978; Zambia – Request for Trust Fund Loan. *TR/78/19*, 4/18/1978. IMF Archives.

objectives of the SNDP [second national development plan] was achieved”<sup>428</sup>. The tougher stance was reflected in the tightened conditions of the new SBA. The expansion of domestic credit and sum of arrears were now scrutinised on a quarterly basis. In addition, external borrowing was restricted as well.<sup>429</sup> The substantial loans meant that Zambia had greatly surpassed its quota for loans from the Fund. However, the Fund staff felt that the exemption was justified, because of the “exceptional circumstances applicable in the case of Zambia”<sup>430</sup>.

A Fund mission visited Lusaka in the end of 1978 to evaluate the stabilisation effort under the SBA. The report was optimistic, noting that the Zambian authorities had largely followed proposed policies and respected the conditions set out by the Fund.<sup>431</sup> Most of the internal targets of the plan were achieved, but on the external side difficulties persisted, as only a small improvement in the balance of payments position was recorded.<sup>432</sup> The report concluded that “in 1978 Zambia’s performance under the current stand-by arrangement clearly demonstrates the Government’s commitment to the program and its resolution to solve the serious economic problems facing the country”<sup>433</sup>.

The first half of 1979 witnessed substantial progress in the external situation, because of a rise in the copper price and the reopening of the Southern transport route through Rhodesia.<sup>434</sup> Domestically, however, serious problems were surfacing and the initial optimism within the Fund was starting to wane. The implementation of the Fund-promoted liberal pricing policies proved hard in the state-led economic model of Zambia and its emphasis on parastatal companies. A prime example of this were the massive

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<sup>428</sup> ZAMBIA – STAFF REPORT AND PROPOSED DECISION FOR THE 1977 ARTICLE XIV CONSULTATION, 4. *SM/78/107*, 4/18/1978. IMF Archives.

<sup>429</sup> ZAMBIA – REQUEST FOR A STAND-BY ARRANGEMENT, 15–16. *EBS/78/190*, 4/19/1978. IMF Archives.

<sup>430</sup> ZAMBIA – REQUEST FOR A STAND-BY ARRANGEMENT, 18. *EBS/78/190*, 4/19/1978. IMF Archives.

<sup>431</sup> ZAMBIA – REVIEW AND CONSULTATION UNDER STAND-BY ARRANGEMENT, 22–24. *EBS/79/194*, 4/2/1979. IMF Archives.

<sup>432</sup> ZAMBIA – REVIEW AND CONSULTATION UNDER STAND-BY ARRANGEMENT, 4. *EBS/79/194*, 4/2/1979. IMF Archives.

<sup>433</sup> ZAMBIA – REVIEW AND CONSULTATION UNDER STAND-BY ARRANGEMENT, 22. *EBS/79/194*, 4/2/1979. IMF Archives.

<sup>434</sup> ZAMBIA – STAFF REPORT FOR THE 1979 ARTICLE IV CONSULTATION, 9. *SM/79/222*, 8/17/1979. IMF Archives.

losses incurred by the National Agricultural Marketing Board (NAMBOARD), a parastatal body in charge of buying, storing and selling agricultural products.<sup>435</sup>

The government had to cover the losses, which meant breaching the first performance criterion of the SBA. In response to a far-reaching pricing plan presented by the Zambian authorities, the Fund approved some modifications to the ceilings of the first condition.<sup>436</sup> Despite the setbacks, the Fund seemed comparatively happy with the Zambian performance during the two years of adjustment under the SBA. A later evaluation did, however, state that “inadequate progress was made in major areas, such as in the reduction of consumer subsidies and the implementation of economic pricing in the important parastatal sector”<sup>437</sup>.

The Bank’s eagerness to lend to Zambia seems to have declined somewhat in the latter part of the 1970s and even more so in the early 1980s. While nine new projects were introduced between 1975 and 1979, the financial weight of the schemes was moderate. Even without taking inflation into account, the loan sums were smaller in absolute terms than before. While some financially substantial infrastructure projects were initiated – most notably a telecommunications project in 1975 (32 million dollars), a highway project in 1978 (22.5 million) and a railway project in 1979 (40 million) – the vast scale of the earlier hydroelectric projects, for example, was not replicated.<sup>438</sup>

In September 1976, when the rapidly deteriorating economic situation of Zambia was fully realised, the Bank issued a 30-million-dollar program loan for the UNIP government. The loan was approved soon after the short-lived SBA was negotiated with the Fund. At the time, the Bank seemed very committed to Zambian development and sensitive to its economic distress, as three special missions had visited the country between September 1975 and April 1976. The program loan had two goals. Firstly, it was directed at helping the government to finance acutely needed imports. Secondly, the Bank hoped that it would help the government to channel investment to the agricultural sector

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<sup>435</sup> ZAMBIA – STAFF REPORT FOR THE 1979 ARTICLE IV CONSULTATION, 9. *SM/79/222*, 8/17/1979. IMF Archives.

<sup>436</sup> ZAMBIA – REQUEST FOR MODIFICATION OF PERFORMANCE CRITERIA UNDER STANDBY ARRANGEMENT, 8–9. *EBS/79/573*, 10/11/1979. IMF Archives.

<sup>437</sup> ZAMBIA – REQUEST FOR EXTENDED ARRANGEMENT, 4. *EBS/81/91*, 4/20/1981. IMF Archives.

<sup>438</sup> World Bank website, 9 March 2019. *Where We Work / Zambia / All Projects*.

in order to diversify the economy.<sup>439</sup> Following the shifting intellectual orientation of the institution, the president's report highlighted that "the Bank's future lending program will emphasise agricultural and rural development to help diversify the economy and improve the living conditions of the rural poor"<sup>440</sup>.

The evaluation report of the loan is rather ambiguous in character. While noting that the program loan was vital in the first objective of financing acute imports, the long-term goal of investing in rural development had largely not materialised. A part of the problem was that the loan had been designed on the assumption that the Zambian government would go through with the SBA and thus secure full credit from the Fund.<sup>441</sup> However, the report stated that "it is difficult, even in retrospect, to argue that the Bank's loan should have been directly linked to drawings under the IMF stand-by"<sup>442</sup>. This was explained by the different goals of the institutions as the Fund was striving for short-term stabilisation and the Bank had its eyes on longer-term structural diversification. Interestingly, the Bank-report seems to imply that this created a conflict of interests between the IFIs in the case of Zambia:

"On the other hand, it is apparent that the strengthening of agricultural services desired by the Bank was not fully compatible with short-term budgetary constraints and the related austerity measures imposed by the IMF, unless the Government was willing to make matching cutbacks elsewhere. While the Fund was trying to impose "across the board" budgetary cuts, the Bank clearly attempted to foster a reallocation of resources among the different budget categories."<sup>443</sup>

The paragraph exposes a lack of co-ordination between the IFIs at the time. Although the Bank waited for the Fund to reach an agreement first, it is clear that the IFIs had different emphases in Zambia. The Bank's concern was in sustaining the path to development, not just in correcting balance of payments imbalances. This is in stark contrast to later years, when the IFIs co-operated closely with the American government playing a crucial part as the facilitator of this liaison.

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<sup>439</sup> World Bank 1976b, 12–14. *Zambia – Small and Medium Scale Industry Development Project (English)*. World Bank Archives.

<sup>440</sup> World Bank 1976b, 17. *Zambia – Small and Medium Scale Industry Development Project (English)*. World Bank Archives.

<sup>441</sup> World Bank 1978, 26–28. *Zambia – Small and Medium Scale Industry Development Project (English)*. World Bank Archives.

<sup>442</sup> World Bank 1978, 27. *Zambia – Small and Medium Scale Industry Development Project (English)*. World Bank Archives.

<sup>443</sup> World Bank 1978, 11. *Zambia – Small and Medium Scale Industry Development Project (English)*. World Bank Archives.

While the IFIs clearly had conflicting views, a co-ordinated international effort was nevertheless desired by the Bank. It sponsored the Zambia Consultative Group (ZCG)<sup>444</sup>, which met in Paris in the summer of 1978. After extensive negotiations, international aid pledges were made and an additional 57-million-dollar loan was secured from the Eurodollar markets. The loan disbursements were linked to Zambia's performance under the 1978 SBA, which surely enhanced the Zambian determination to see through the stabilisation program. In addition, the Bank established a committee in charge of managing the external debts of Zambia.<sup>445</sup>

In late 1979, the UNIP government had announced the third national development program for the years 1979–1983. The second national development plan had failed, and because of its over-optimistic goals the UNIP government was losing credibility in the IFIs. While the Bank had wanted to support the second plan, it was brutally frank about the third plan in its evaluation:

"The TNDP is weak first, because it has not adequately accounted for the effects of the prolonged economic and financial crisis, second, because its assumptions regarding resource availability are too optimistic, especially for the Government sector, and finally because it does not set out the strategies and procedures which planners and plan implementers should follow in the event that assumed resources do not materialize."<sup>446</sup>

This extract is telling as it displays the change in the Bank's standpoint in relation to Zambia. At the time of the commodity price shock in 1974, the Bank was dedicated to the development agenda in Zambia. It was willing to keep lending to the country, because it believed in Zambia's progress and ability to endure the acute crisis. In the following few years this commitment seems to have evaporated as the economic situation in Zambia worsened. Moreover, as the citation above testifies, the Bank lost its faith in the UNIP government's capability to formulate economic policies. The Bank staff toned down their rather unconditional pledges to support Zambian development and did not question the Fund's austerity measures like they had back in 1976. Instead, in the midst of the debt

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<sup>444</sup> In addition to the Zambian authorities and the IFIs, the ZCG included delegates from the developed countries and private financiers. Similar negotiations were held later in the framework of the so-called Paris Club, where the IFIs (regional development banks included) acted as mediators in negotiations between creditor countries and indebted countries. The Paris Club had meetings with the Zambian authorities four times in 1983–1990. The three first meetings focused on debt rescheduling, while the last meeting included debt relief. (Fernholz 2004, 266–268).

<sup>445</sup> ZAMBIA – REVIEW AND CONSULTATION UNDER STAND-BY ARRANGEMENT, 22–24. EBS/79/194, 4/2/1979. IMF Archives.

<sup>446</sup> World Bank 1981a, 21. *Zambia – Country economic memorandum (English)*. World Bank Archives.



crisis, the long-term goal of diversifying the Zambian economy became the focal point of the Bank's policies. Program and sector-specific loans were increasingly applied to achieve this target.

Compared to the Bank, the Fund approached the problems in Zambia strictly from an economic perspective. The institution's operations were largely guided by the neoclassical paradigm of sustaining internal and external macroeconomic balances. Although it was not until the strong American push for control started in the 1980s that the Fund became a fully-fledged herald of the neoliberal dogma, a gradual change in the emphasis of its policies can be traced already during the 1970s. In the first years of the crisis, the focus was on traditional austerity measures, as slashing government expenditures and controlling the expansion of credit were common policies. While the targets of achieving financial equilibrium and curbing indebtedness remained the same, the set of policies designed to obtain these goals widened. The liberalisation of prices and capital transactions and the removal of subsidies gained steadily more importance in the Fund's programs. Overall, however, conditionality was still quite weak in these years.

In many ways, the five years or so after the copper price crash, are crucial in explaining the economic woes of Zambia. The years had far-reaching consequences, because of the rapid accumulation of debt. Furthermore, the economic catastrophe of later years could have been averted by taking rigorous corrective actions following the copper price crash. The main culprit here was the Zambian government, which did not cut domestic consumption, but rather, sustained it by borrowing more. In hindsight, the failure to adjust the economy looks inexcusable, but it has to be remembered, that the fall in copper prices was expected to be a temporary difficulty.

In my opinion, the reasonableness of the IFI's policies in Zambia during the late 1970s should be questioned somewhat. Both institutions kept providing funds to a country that was clearly in a spiral of escalating indebtedness. Zambia had trouble in repaying its loans already in 1975 and just three years later its debt amounted to a half of the GDP, a very high figure at the time.<sup>447</sup> Once again, the lavish lending was based, at least partially, on the assumption that copper prices would recover quickly. Nevertheless, especially when

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<sup>447</sup> McPherson 2004a, 38.

taking into account the IFI's later strictness, the continued lending seems problematic in retrospect.

Paradoxically, the limited scope of US influence and the relatively low conditionality probably contributed to the exacerbation of the troubles of Zambia. At a time when the Bank and the Fund were enjoying relative autonomy, the IFIs were unable to decisively help the Zambian economy out of the slump. On the contrary, the IFIs kept providing new resources, with few conditions attached, to an incompetent Zambian government, which failed in the implementation of most of the programs. In this process, the Zambian government became accustomed to turning to the IFIs for aid, despite routinely providing disappointing results in the execution of the jointly negotiated programs.

In the latter part of the 1970s the IFIs were in a state of transformation. The Fund was marginalised by the US government but increasingly engaged in struggling developing countries. In contrast, the Bank had established itself as a credible promoter of development issues, but looking after the macroeconomic balance of indebted developing countries was not yet a central part of its function. Speculatively thinking, stronger IFIs at the time could have imposed tougher conditions on the Zambian government and thus helped it in guiding the economy towards the needed adjustments. The economic liberalisation and loss of autonomy that this would have entailed can be debated, but, in the absence of such determination, the IFIs contributed mainly to a sustaining of the status quo while external debts kept accumulating. The absence of committed external political guidance is also visible in the evident lack of co-ordination between the IFIs at the time, demonstrated by the conflicting priorities in adjusting the Zambian economy.

### 3.4 The Collapse and Insolvency: 1980–1985

After the establishment of the one-party state in 1972, political opposition in Zambia disappeared largely underground. The internal conflict in the UNIP party, which had led to the banning of Simon Kapwepwe's offshoot UPP-party, shaped the political environment for years to come. Many of the UPP-supporters re-joined UNIP. The rationale behind this was the belief that working the system from the inside would bring better results than direct confrontation with the state. The ones who sought to topple Kaunda and his party from the grass root level had to gather in secret and under an increasing threat of repression. The dissidents organised meetings in imaginative settings, like family gatherings, church ceremonies and cultural events. The split in the ruling party carried long-lasting effects, as the UNIP leadership's legitimacy started to crumble in the eyes of the broader public. The party lost support among voters in its core areas: the Copperbelt and Northern Province. In an act of reconciliation Kaunda accepted Kapwepwe back into UNIP in 1977, only to imprison him on dubious charges soon after, because the rival had declared his intentions to challenge the sitting president.<sup>448</sup>

In the late 1970s, the future president of the country, Frederick Chiluba, started to gain more political clout. His vehicle for organising support were trade unions, in which the UNIP government's economic policies were viewed increasingly with dismay.<sup>449</sup> The political climax of these years was seen in October 1980 when a coup attempt was pre-empted. A group of wealthy businessmen were behind the plot, and they had support from Zairean rebels. Dozens of influential Zambian figures were sent to jail and seven of the conspirators were sentenced to death, but Kaunda pardoned them later in 1990.<sup>450</sup> The internal uprising raised concern for the UNIP party in a comprehensive way, because it coincided with Zimbabwe gaining independence. The end of the Rhodesian white settler rule meant that the biggest external threat to Zambian security vanished, which in turn provoked criticism towards the ruling party as calls for a democratic transition were made.<sup>451</sup> Moreover, Kaunda was convinced that the plotters enjoyed the tacit support of South Africa and its intelligence services. Later research has confirmed that no evidence supporting South African meddling exists. However, they did help in a failed attempt to

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<sup>448</sup> Larmer 2008, 106–114.

<sup>449</sup> Mulenga 2008, 246.

<sup>450</sup> Larmer 2008, 114, 119.

<sup>451</sup> Larmer 2008, 118.

free the prisoners next year.<sup>452</sup> As a result of the tensions, Zambia's defence expenditures were pushed up at a time when the state really could not afford it.<sup>453</sup>

To compound the political pressures, the economic situation was getting rapidly worse again. After the relatively successful stabilisation process in 1978–1979, the new decade started in a desperate atmosphere. Large parts of Zambia suffered from droughts in 1979, 1981 and 1983, which meant that a significant portion of the yearly consumption of maize (the staple food product in Zambia) had to be imported.<sup>454</sup> The droughts proved to be a turning point for the agricultural sector as per capita production declined through the 1980s and the 1990s.<sup>455</sup>

During these years debt repayment became increasingly difficult. One reason behind this was the Volcker shock, after which interest rates climbed up around the world with severe consequences for indebted countries. In fact, Fernholz lists the interest rate hikes as the fourth and final external shock that hit Zambia after independence.<sup>456</sup> The UNIP government reacted by levying even tighter controls on capital transactions. Creditors demanded guarantees on their loans and this prompted the Zambian government to switch a big share of the unsettled loans to public sector debt. The Zambian foreign exchange reserves diminished until the country was practically default by 1987.<sup>457</sup>

In April 1981, the Zambian authorities requested an 800 million SDR loan from the Extended Fund Facility (EFF) that would be phased over three years.<sup>458</sup> The Zambian authorities drew up a financial program for the years 1981–1983. Here, it is important to note, that while the staff of the IFIs (in Fund documents especially) portray these programs as products of the Zambian authorities, they clearly influenced them a lot. The staff of both IFIs had regular discussions with the Zambian government. In my opinion, it is evident that it was in the interest of the IFIs to highlight the Zambian ownership of

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<sup>452</sup> Larmer 2008, 120–121.

<sup>453</sup> ZAMBIA – REQUEST FOR EXTENDED ARRANGEMENT, 7. *EBS/81/91*, 4/20/1981. IMF Archives; World Bank 1981a, 21. *Zambia – Country economic memorandum (English)*. World Bank Archives.

<sup>454</sup> McPherson 2004b, 300; ZAMBIA – REVIEW AND CONSULTATION UNDER STAND-BY ARRANGEMENT, 5. *EBS/80/53*, 3/17/1980. IMF Archives.

<sup>455</sup> McPherson 2004a, 33.

<sup>456</sup> Fernholz 2004, 264–265. The first shock was the UDI of Southern Rhodesia and subsequent tensions in Zambia's neighbouring countries, which caused transportation issues and hampered trade. The second was the oil crisis, which increased the cost of oil imports significantly. The third shock was the copper price crash and its devastating effects on Zambia's balance of payments position.

<sup>457</sup> Fernholz 2004, 265.

<sup>458</sup> ZAMBIA – REQUEST FOR EXTENDED ARRANGEMENT. *EBS/81/91*, 4/20/1981. IMF Archives.

the programs so that their own influence and pressure would not stand out. The bottom line is that, in order to secure funds from the IFIs, the Zambian government had to present programs that were approved by them. Thus, the policies that are presented as creations of the Zambian government represent to a large extent the aspirations of the IFIs.

The aim of the adjustment program in 1981–1983 was to halt the contraction of the economy by diversifying productive capacities and achieving a healthy annual growth rate of five per cent. On the fiscal side austerity was endorsed, as the goals of the program were to achieve equilibrium domestically and a sustainable position externally. Investment was to be channelled to productive sectors of the economy, agriculture in particular. Special attention was given to pricing policies. Government subsidies were to be reduced significantly or eliminated entirely.<sup>459</sup> The Fund report noted the political sensitiveness of these policies:

“While it is recognized that price increases affecting particularly the urban population are not easy to carry out from a political point of view, it will be necessary to make further progress during the program period”<sup>460</sup>.

Although just four conditions were outlined in the EFF loan and, moreover, they were almost identical to the performance criteria of the previous SBA, the 1981 adjustment program differed crucially from its predecessor.<sup>461</sup> In their suggested program the Zambian authorities emphasised the need to implement policies targeted at fixing medium-term issues, and these policies were discussed in the lengthy memorandum in detail. Moreover, the EFF was designed to help in lengthier adjustments compared to the stabilisation efforts of the SBAs. Thus, the 1981 adjustment program truly earned the prefix, “structural”, as it was increasingly aimed at correcting underlying problems of the economy, not just acute liquidity issues. Fund staff noted this with approval: “for the first time the Government's medium-term priorities are set out in an operationally relevant document”<sup>462</sup>.

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<sup>459</sup> ZAMBIA – REQUEST FOR EXTENDED ARRANGEMENT, 9–11. *EBS/81/91*, 4/20/1981. IMF Archives.

<sup>460</sup> ZAMBIA – REQUEST FOR EXTENDED ARRANGEMENT, 31. *EBS/81/91*, 4/20/1981. IMF Archives.

<sup>461</sup> ZAMBIA – REQUEST FOR EXTENDED ARRANGEMENT, 25–27. *EBS/81/91*, 4/20/1981. IMF Archives.

<sup>462</sup> ZAMBIA – REQUEST FOR EXTENDED ARRANGEMENT, 13. *EBS/81/91*, 4/20/1981. IMF Archives.

The 1981 EFF loan introduced a first real co-ordinated effort on the behalf of the IFIs in the context of Zambia. The UNIP government's investment plan was reviewed by staff members of both institutions and discussed together with all three parties<sup>463</sup> Just two weeks after the Zambian authorities had reached an agreement with the Fund officials, the Bank provided two sectoral loans (11 and 18 million dollars), targeted at boosting agricultural production in the Eastern and Southern provinces respectively.<sup>464</sup> Compared to the late 1970s, the division of work between the IFIs was more clearly outlined and the goals of the SAP more broadly shared. The Fund supplied the bulk of the resources for the immediate adjustment and the Bank assisted by providing additional loans that were targeted on the longer-term goal of diversifying the economy.

Implementation of the SAP proved difficult from the very beginning. Early warning signs were seen in November 1981, when Zambia had to request for a waiver, as its external arrears exceeded the limit set by the Fund.<sup>465</sup> At the end of the year, it was clear that it could not meet the conditions, and in July 1982, the Zambian authorities cancelled the program. 300 million SDR had been disbursed prior to the dissolution of the SAP.<sup>466</sup> A major reason for the poor performance was that the projected trends of copper prices proved to be too optimistic. After gradually picking up again in the last years of the 1970s, a steady decline from February 1980 to the summer of 1982 wiped 55 per cent of the value of the commodity.<sup>467</sup> As export revenues tumbled, the Zambian request for 59.3 million SDR from the CFF was approved by the Fund in 1981. Although the EFF-loan was cancelled in July 1982, the Fund approved another CFF-loan later that year, worth 34 million.<sup>468</sup>

Despite the cancellation, the parties remained in close contact as discussions for a new adjustment program were initiated almost instantly. The state of the Zambian economy

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<sup>463</sup> ZAMBIA – REQUEST FOR EXTENDED ARRANGEMENT, 13. *EBS/81/91*, 4/20/1981. IMF Archives.

<sup>464</sup> World Bank 1981b. *Zambia –Eastern Province Agricultural Development Project (English)*; World Bank 1981c. *Zambia – Southern Province Agricultural Development Project (English)*. World Bank Archives.

<sup>465</sup> ZAMBIA – REQUEST FOR WAIVER AND MODIFICATION OF PERFORMANCE CRITERION UNDER EXTENDED ARRANGEMENT. *EBS/81/220*, 11/6/1981. IMF Archives.

<sup>466</sup> ZAMBIA – USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 3. *EBS/82/212*, 11/23/1982. IMF Archives.

<sup>467</sup> Boos & Holm-Müller 2016, 895.

<sup>468</sup> ZAMBIA – USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 10–11. *EBS/81/194*, 9/25/1981; ZAMBIA – USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY. *EBS/82/212*, 11/23/1982. IMF Archives.

was deteriorating alarmingly on many different fronts. The most acute problem was the shortage of foreign exchange, which threatened the Zambian government's solvency and stifled investments in the newly established giant mining company, the Zambia Consolidated Copper Mines (ZCCM), and other vital sectors of the economy. In addition, inflation was gathering pace: A Fund report estimated that consumer prices for low-income groups rose nearly 20 per cent in 1983.<sup>469</sup> The unsustainable situation required radical measures. In January, the Zambian authorities announced a 20 per cent devaluation of the kwacha and a temporary suspension of payments of arrears, as well as of principals of external loans.<sup>470</sup> In May 1983, an agreement was reached on substantial rescheduling of existing Zambian debt in a Paris Club meeting with the country's main creditors.<sup>471</sup>

The negotiations for a new SAP were concluded in April 1983 before the Paris Club meeting. Reflecting a change in the Fund's approach, the new program was a SBA (211.5 million SDR) for one year. It was supplemented with a significant loan (97.2 million SDR) from the CFF.<sup>472</sup> The binding conditions of the SBA were similar to previous loans, mainly aimed at curbing debt and stabilising the government budget and balance of payments.<sup>473</sup> However, the failures of the earlier arrangements seem to have affected the Fund's tactics, because they requested an evaluation for June, just three months into the program. Moreover, in addition to reviewing the performance criteria, other policies included in the program were to be evaluated as well:

“In particular, this review will require understandings to be reached with the Fund on performance criteria for the remaining period of the program, as well as on exchange rate and interest rate policies. Other topics of the review will include progress on debt rescheduling, budgetary performance, credit policies, and prices and incomes policies.”<sup>474</sup>

A comparison of the SAPs of 1981 and 1983 is informative. Firstly, it indicates the graveness of the troubles facing Zambia. By 1983, the country was in a position were at

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<sup>469</sup> ZAMBIA – RECENT ECONOMIC DEVELOPMENTS, 5, 21. *SM/84/125*, 6/1/1984. IMF Archives.

<sup>470</sup> ZAMBIA – EXCHANGE ARRANGEMENTS, 1. *EBS/83/10*, 1/11/1983. IMF Archives.

<sup>471</sup> REPORT ON ZAMBIA'S EXTERNAL DEBT RENEGOTIATION. *SM/83/106*, 5/26/1983. IMF Archives.

<sup>472</sup> ZAMBIA – USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY. *EBS/83/70*, 3/31/1983. IMF Archives.

<sup>473</sup> ZAMBIA – STAFF REPORT FOR THE 1982 ARTICLE IV CONSULTATION AND REQUEST FOR STAND-BY ARRANGEMENT, 29. *EBS/83/67*, 3/30/1983. IMF Archives.

<sup>474</sup> ZAMBIA – STAFF REPORT FOR THE 1982 ARTICLE IV CONSULTATION AND REQUEST FOR STAND-BY ARRANGEMENT, 29. *EBS/83/67*, 3/30/1983. IMF Archives.

the same time it desperately needed both external resources and comprehensive structural reforms. While the ambitious EFF loan in 1981 had targeted economic growth and the diversification of the economy, the financial program<sup>475</sup> of 1983 was clearly aimed at fixing the former problem. The second observation is the change in the Fund's approach. The SAP in 1983 spanned over just one year, and instead of boldly targeting the diversification of the economy, its aim was rather to build the basis for this objective.<sup>476</sup> Diversification was still seen as an essential goal, but the problems facing Zambia were now to be tackled in a chronological order, as the minutes of an executive board meeting reveal:

“The staff could agree that there was such a need, but in the present circumstances, given the foreign exchange crisis, the highest priority surely had to be setting the country's financial house in order. Once the authorities had done that, they would find it far easier to concentrate on diversification efforts.”<sup>477</sup>

A few different factors are likely to have influenced the SBA. The succession of failed programs of the Zambian government made a shorter adjustment program a more attractive option. It is probable that the debt crisis, which had spread globally in the autumn of 1982, also had an effect. The US started propagating for a more influential role for the Fund and the institution got a new injection of funds the next year. During the acute phase of the crisis, the Fund's focus was on short-term liquidity issues. The rationale was to give indebted countries more resources to endure the immediate crisis, but full repayment of the loans was nevertheless expected.

Interesting minutes of an executive board meeting discussing Zambia's situation in April 1983 can be found in the Fund's archives. Two officials – the executive director of the US, Charles Dallara, and his colleague from the UK, Christopher Taylor – stand out with their lengthy assertions. Both directors emphasised in their statements the importance of austerity and price liberalisation in the Zambian case. Taylor stressed that “it would also be necessary for producer prices to continue to convey significant market-related

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<sup>475</sup> While this particular program did not alter from its predecessors in a significant way, it was called financial program, stressing the emphasis of the plan.

<sup>476</sup> ZAMBIA – STAFF REPORT FOR THE 1982 ARTICLE IV CONSULTATION AND REQUEST FOR STAND-BY ARRANGEMENT, 15. *EBIS/83/67*, 3/30/1983. IMF Archives.

<sup>477</sup> ZAMBIA – 1982 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT, AND USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 29. *EBM/83/63-1 – Final*, 4/18/1983. IMF Archives.



incentives”<sup>478</sup>, while Dallara noted that “it was particularly important to keep expenditure within agreed limits”<sup>479</sup>.

One point of major conflict can be found in the discussion. Taylor and Dallara supported the Fund management’s proposal to wait for the Paris Club negotiations – scheduled later in May – before approving the substantial CFF-loan. The rationale behind this sequence of actions was that, for Zambia, securing additional external funds was seen as vital for carrying out the SAP.<sup>480</sup> Many of the other directors expressed their apprehensions of the proposed extra conditionality, because the disbursement of CFF-funds was supposed to be guided by the simple principle of supporting countries suffering temporary falls in export earnings.<sup>481</sup> While Taylor was maintaining that the procedure was an exception due to the unique predicaments of Zambia, Dallara declared that “there were some questions as to whether the Fund could have reasonable assurances that its resources would be repaid on schedule”<sup>482</sup>. Dallara justified his view by emphasising that, in the Zambian case, drops in export revenues had not proven to be temporary in nature, and by implying that the Fund had provided resources with inadequate precautions to Zambia in previous years.<sup>483</sup>

Unsurprisingly, the executive board decided to follow the management’s recommendation and the CFF-loan was not approved before additional funds and the rescheduling of debt were secured at the Paris Club meeting.<sup>484</sup> The minutes reveal the tightening conditionality and liberalising policies that the Americans pushed for in the

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<sup>478</sup> ZAMBIA – 1982 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT, AND USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 7. *EBM/83/63-1 – Final*, 4/18/1983. IMF Archives

<sup>479</sup> ZAMBIA – 1982 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT, AND USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 16. *EBM/83/63-1 – Final*, 4/18/1983. IMF Archives

<sup>480</sup> ZAMBIA – 1982 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT, AND USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 8–9. *EBM/83/63-1 – Final*, 4/18/1983. IMF Archives.

<sup>481</sup> ZAMBIA – 1982 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT, AND USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 11, 23, 28. *EBM/83/63-1 – Final*, 4/18/1983. IMF Archives.

<sup>482</sup> ZAMBIA – 1982 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT, AND USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 19. *EBM/83/63-1 – Final*, 4/18/1983. IMF Archives.

<sup>483</sup> ZAMBIA – 1982 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT, AND USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 27. *EBM/83/63-1 – Final*, 4/18/1983. IMF Archives.

<sup>484</sup> ZAMBIA – USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 1. *EBS/83/70*, 5/18/1983. IMF Archives.

Fund at the time. Moreover, while it was recognised that Zambia urgently needed temporary debt relief, the rescheduling of some of the payment arrears was the absolute limit for the Americans. According to the minutes, “Mr Dallara stated, the need to safeguard the revolving nature of the Fund’s resources was paramount”<sup>485</sup>. The minutes are informative in other aspects as well. Taylor and Dallara both supported the Bank’s involvement in longer term structural adjustment by drafting an investment program in collaboration with the Zambian authorities.<sup>486</sup> This was in line with the US government’s position at the time, as the aim was to assign distinct roles for the IFIs in handling the debt crisis.

In its mid-term evaluation of the SAP, the Fund listed with satisfaction the adjustment measures that the Zambian government had undertaken:

“Under the present stand-by arrangement, the Zambia” authorities have made substantial progress in implementing adjustment measures. These have included importantly a significant depreciation of the kwacha and the adoption of a rare flexible exchange rate policy, an upward adjustment in interest rates, a wide range of tax increases, sizable increases in the retail prices of maize and fertiliser and agricultural producer prices, and a general decontrol of wholesale and retail prices. There has also been a vigorous and successful effort to reduce costs in the important mining sector.”<sup>487</sup>

Despite the laborious efforts and meeting all the conditions of the program, the Zambian financial position did not recover as expected. The Zambian representative in the Fund’s executive board, N’Faly Sangare, assigned the disappointing results to severe shortages of foreign reserves, caused by transport problems in shipping exports. Domestically, a fall in imports and a decline in overall economic activity meant that raising projected amounts of revenue proved impossible.<sup>488</sup> In July 1983, the Zambian authorities made further attempts to fix the situation. A flexible exchange rate was adopted, and the kwacha quickly depreciated over ten per cent against the dollar. In addition, the mineral exports

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<sup>485</sup> ZAMBIA – 1982 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT, AND USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 19. *EBM/83/63-1 – Final*, 4/18/1983. IMF Archives.

<sup>486</sup> ZAMBIA – 1982 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT, AND USE OF FUND RESOURCES – COMPENSATORY FINANCING FACILITY, 8, 19. *EBM/83/63-1 – Final*, 4/18/1983. IMF Archives.

<sup>487</sup> ZAMBIA – MIDTERM REVIEW OF THE STAND-BY ARRANGEMENT, 20. *EBS/83/176*, 8/18/1983. IMF Archives.

<sup>488</sup> Statement by Mr. Sangare on Zambia – *EBM/83/141* (9/16/83), 1–2. *BUFF/83/243*, 9/15/1983. IMF Archives.

tax was doubled.<sup>489</sup> The expected competitiveness boost after the depreciation of the currency never materialised, as global demand of copper remained low.<sup>490</sup>

Yet again, the SAP was not carried through. The last disbursement of 67.5 million SDR was cancelled, because “the shortage of foreign exchange led to the criteria on arrears under debt rescheduling agreements and on commercial payments being exceeded”<sup>491</sup>. The Fund report did, however, highlight the rigorous efforts of the Zambian authorities, which justified a new SBA loan, approved in July 1984.<sup>492</sup> The new SAP stretched to April 1986 and was worth 225 million SDR. For the first time, the official list of conditions exceeded ten items. While most of the performance criteria touched the familiar issues of credit control and management of payment arrears, more emphasis was placed on the Fund staff’s reviews of the program.<sup>493</sup> The first review of the program was scheduled as early as September and was catered to “deal in particular with external debt rescheduling, exchange rate policy, and budgetary developments”<sup>494</sup>.

Moreover, the financial program that was devised with the Zambian authorities was rich in detail. For example, it contained a 0.08 kwacha rise in the price of a bottle of beer.<sup>495</sup> This reflects the change towards “micro-conditionality” that was taking place in the Fund. While the previous programs, especially in the 1970s, had highlighted the importance of price liberalisation, for example, the SAP of 1984 had very specific policy measures outlined in it. In my opinion, it reflects the fact that Zambia was gradually losing its economic self-governance. The country was in a position, where Fund officials could compel the Zambian authorities to undertake very explicit measures.

At a quick glance, the Bank seems to have concentrated on active and miscellaneous project lending in Zambia during these years, with as many as sixteen different projects

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<sup>489</sup> ZAMBIA – STAND-BY ARRANGEMENT – MIDTERM REVIEW, 10–12. *EBM/83/142-2 – Final*, 9/16/1983. IMF Archives.

<sup>490</sup> ZAMBIA – REVIEW UNDER STAND-BY ARRANGEMENT, 4. *EBM/84/3-2 – Final*, 1/9/1984. IMF Archives.

<sup>491</sup> ZAMBIA – STAFF REPORT FOR THE 1984 ARTICLE IV CONSULTATION AND REQUEST FOR STAND-BY ARRANGEMENT, 5. *EBS/84/135*, 6/21/1984. IMF Archives.

<sup>492</sup> ZAMBIA – STAFF REPORT FOR THE 1984 ARTICLE IV CONSULTATION AND REQUEST FOR STAND-BY ARRANGEMENT, 39–40. *EBS/84/135*, 6/21/1984. IMF Archives.

<sup>493</sup> ZAMBIA – STAFF REPORT FOR THE 1984 ARTICLE IV CONSULTATION AND REQUEST FOR STAND-BY ARRANGEMENT, 30. *EBS/84/135*, 6/21/1984. IMF Archives.

<sup>494</sup> ZAMBIA – STAFF REPORT FOR THE 1984 ARTICLE IV CONSULTATION AND REQUEST FOR STAND-BY ARRANGEMENT, 30. *EBS/84/135*, 6/21/1984. IMF Archives.

<sup>495</sup> ZAMBIA – STAFF REPORT FOR THE 1984 ARTICLE IV CONSULTATION AND REQUEST FOR STAND-BY ARRANGEMENT, 20. *EBS/84/135*, 6/21/1984. IMF Archives.

introduced in 1980–1985. However, this hides the fact that structural adjustment lending was steadily gaining more importance in the Zambian loan portfolio. First of all, most of the new projects were significantly smaller in size than before, probably reflecting the grave economic situation in Zambia. The notable exceptions were a fifth education project in 1982 (25 million dollars), a rural water supply project in 1983 (16 million), a third industrial forestry project in 1984 (22.5 million) and a railway project in 1985 (20 million).<sup>496</sup>

While the two sectoral loans to agriculture in 1981 had been rather modest in size, especially in comparison to the Fund's concurrent EFF loan, the Bank gradually gained a bigger role in the adjustment process of Zambia. At the onset of the global debt crisis, the immediate focus of the international financial community was on acute stabilisation, following the co-ordinated lead of the US Treasury and the Fund. Pretty soon the need for longer-term structural adjustment gained more prominence, presumably because in many countries (Zambia included) the quick fix had not led to results to speak of.

If the Fund was a co-ordinator for financiers in arranging debt repayment and additional funds for stabilisation, the Bank took on a similar role in Zambia as the organiser of funding for longer-term adjustment. In May 1984, the Bank chaired the Zambia Consultative Group (ZCG) meeting in Paris. The main objective of the meeting was to draw up an investment plan for Zambia and negotiate multi-donor loans to support the diversification of the economy. The first multi-donor loan – for an export rehabilitation and diversification project – had already been approved before the ZCG-meeting in March 1984. The loan's aim was the rehabilitation of the ailing mining sector and the national mining company, ZCCM. In total, the investment amounted to 300 million dollars, with the Bank providing 75 million and the European Economic Community (EEC) and the African Development Bank (AfDB) supplying 46 million and 27 million respectively. The other half of the sum was to be raised through ZCCMs internal cash generation.<sup>497</sup> Similar rehabilitation loans on a smaller scale were issued to the

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<sup>496</sup> World Bank website, 4 April 2019. *Where We Work / Zambia / All Projects*.

<sup>497</sup> World Bank 1984a, ii, 1. *Zambia – Export Rehabilitation and Diversification Project (English)*. World Bank Archives.

agricultural sector (72,3 million dollars, of which the Bank provided 25 million) and to the industrial sector (62 million, with the Bank's share being 20 million).<sup>498</sup>

Although the Bank highlighted the need to diversify the productive capacities of the Zambian economy, regaining the lost productivity of the mines was seen as an essential first step. Therefore, it can be deduced that the Bank had adopted the same approach as the Fund after the global debt crisis. A Bank report of the export rehabilitation loan spelled out the conviction:

"Paradoxically, policies to lessen Zambia's dependence on copper, and to bring about diversification, have little chance of succeeding without investing first in the rehabilitation of the copper industry. For any long-term growth strategy to succeed, it is of the utmost importance that financial balance in the economy and creditworthiness be restored first."<sup>499</sup>

This extract is in stark contrast to the Bank's proclamations of the 1970s, which had shown confidence in the progress that could be made under a more developmentalist approach in economic policy. The huge problems that most of the developing countries were facing at the time of the debt crisis undoubtedly influenced the change of outlook, but one cannot overlook the spread of neoliberalism, which can be seen in other aspects of the three rehabilitation loans. Prior to the issuing of the rehabilitation loans, the Bank had held extensive consultations with the Zambian authorities for nearly two years. In these discussions, the parties had outlined some medium-term targets for the Zambian economy, which the Bank report summarised as follows:

"Providing a system of incentives to producers and exporters of agricultural and industrial products in which prices are responsive to market forces; Allowing greater competition in the procurement and selling of food crops. Ultimately, NAMBOARD, the Government's agricultural marketing agency, will act only as the buyer and seller of last resort to ensure the effectiveness of incentive pricing; Improving planning, and budgetary and other procedures to shift resources to productive sectors; Using wages and interest rate policies to reverse past trends of increasing consumption and declining investment; Improving the management of foreign debt; Strengthening the technical and managerial capacity of ZIMCO, which is the holding company of most state-controlled enterprises; Restructuring the energy sector to bring about lesser dependence on imported oil; and Ensuring the competitiveness of exports through an active exchange rate policy."<sup>500</sup>

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<sup>498</sup> World Bank 1984b, ii. *Zambia – Agricultural Rehabilitation Project (English)*; World Bank 1985c, 1. *Zambia – Industrial Reorientation Project (English)*. World Bank Archives.

<sup>499</sup> World Bank 1984a, 4. *Zambia – Export Rehabilitation and Diversification Project (English)*. World Bank Archives.

<sup>500</sup> World Bank 1984a, 4. *Zambia – Export Rehabilitation and Diversification Project (English)*. World Bank Archives.

In comparison to the Fund's increasingly detailed SAPs, these measures were more like strategic goals for reforming the economy in the longer time frame. Liberalisation of prices, boosting competition and promoting more flexibility in interest and exchange rate policies were standard principles of the neoliberal thought collective. Thus, although the Bank's operations in Zambia consisted seemingly of issuing sector-oriented loans, it was simultaneously leading an effort to restructure the economy in a more holistic way. In essence, the aim was to dismantle the model of economic nationalisation and state planning, which the Zambian government had adopted since independence. The Fund had vociferously disapproved of many of the "statist" policies already 1970s, but for the Bank this was a more recent undertaking.

The export rehabilitation project was divided to two phases: the first one spanning through 1984–1985, and the second one covering the year 1986. In order to receive the disbursements for the second phase the Zambian government had to meet three conditions.<sup>501</sup> The first two conditions concerned ZCCMs operations, but the third one was more general as it required that "the Borrower has made adequate progress in the carrying out of the actions referred to in the letter from the Minister of Finance"<sup>502</sup>. Interestingly, the annexed letter specified the broad policy targets for the medium term that had been negotiated between the Bank staff and the UNIP government, summarised in the lengthy quotation above.<sup>503</sup> Thus it can be determined, that whereas the Fund's conditionality had been evolving towards the micromanagement of policies, the Bank seems to have adopted a different line. The rehabilitation loans had fewer conditions, but more room for interpretation when evaluating the performance under them.

The export rehabilitation loan had three main elements: recuperation of equipment, training of personnel and rationalisation of mining operations.<sup>504</sup> While the first two objectives raise no further questions, the third component is intriguing in its vagueness. Larmer maintains that the loan was conditioned on cutting the ZCCM-workforce significantly and introducing better discipline at the workplace.<sup>505</sup> The same broad

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<sup>501</sup> World Bank 1984a, 20. *Zambia – Export Rehabilitation and Diversification Project (English)*. World Bank Archives.

<sup>502</sup> World Bank 1984a, 20. *Zambia – Export Rehabilitation and Diversification Project (English)*. World Bank Archives.

<sup>503</sup> World Bank 1984a, 35–43. *Zambia – Export Rehabilitation and Diversification Project (English)*. World Bank Archives.

<sup>504</sup> World Bank 1984a, 18. *Zambia – Export Rehabilitation and Diversification Project (English)*. World Bank Archives.

<sup>505</sup> Larmer 2010, 41.

objective of increasing efficiency was spelled out in the other two rehabilitation loans as well. One of the targets of the agricultural rehabilitation project was to “adopt a policy of economic pricing for parastatal enterprises, and streamline their operations”<sup>506</sup>. Similarly, the industrial reorientation project stated that the Zambian government was committed “to rely increasingly on market forces to allocate resources, and to reduce the share and increase the efficiency of the public sector in manufacturing”<sup>507</sup>.

Indeed, the rehabilitation loans were designed to thoroughly overhaul the parastatal sector of the economy. According to Jonathan Kydd, the Bank and the ZCG believed that because diversification and growth “could only be achieved by policies which rolled back economic controls, it was desired to liberalise as many sectors as possible, and to break-up the monolithic structure of state-owned enterprises”<sup>508</sup>. The full privatisation of state-owned companies was not yet on the Bank’s agenda. However, the Bank did evidently view the parastatal sector as a wasteful and unproductive segment of the economy. Thus, streamlining the parastatal companies was a pivotal component in the effort to diversify the Zambian economy.

If one of the Bank’s central aims was to reform the parastatal sector, the results proved to be disappointing to say the least. According to Larmer, the effort to integrate mining operations under ZCCM actually enabled the Zambian state to hoard more mining revenues as the centralisation fostered corruption.<sup>509</sup> The same message is echoed in the Bank’s evaluation of the loan from 1992:

“ZCCM’s managerial autonomy and accountability were not even considered as a potential issue, given the dominant role of the Party (UNIP) in the management of the economy, the way the appointments of the top executives were made, and the strong sense of party loyalties within the corporate structure. In terms of accountability, ZCCM has been “a state within a state.”<sup>510</sup>

In the summer of 1985 the Zambian economy was on the verge of default. The Fund calculated that Zambian mid- and long-term external debt amounted to over 3.5 billion

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<sup>506</sup> World Bank 1984b, 14. *Zambia – Agricultural Rehabilitation Project (English)*. World Bank Archives.

<sup>507</sup> World Bank 1985c, 16. *Zambia – Industrial Reorientation Project (English)*. World Bank Archives.

<sup>508</sup> Kydd 1988, 237.

<sup>509</sup> Larmer 2010, 41.

<sup>510</sup> World Bank 1992, 19. *Export Rehabilitation and Diversification Project (English)*. World Bank Archives.

dollars.<sup>511</sup> Moreover, it could not pay back its scheduled obligations to the Fund. The Fund decreed that Zambia could not make use of Fund resources before it started paying back its obligations on schedule.<sup>512</sup> Incidentally, the decision was taken in an executive board meeting in Seoul in October 1985, when the Baker Plan was unveiled by the US Treasury. In the face of the deteriorating economic conditions, members of the Fund staff had visited Lusaka back in April 1985, but an agreement with the Zambian authorities for further adjustment measures could not be reached. As a result, the SAP of 1984 was declared inoperative.<sup>513</sup>

Hence, after a stint of comparative prudence in obeying the Fund programs, a change happened in the Zambian government's approach in 1985. One major factor that contributed to the sudden shift was the influence of the domestic political situation. In the 1980s, the trade unions, led by Chiluba, became the main opposition to the UNIP government and one-party politics. The main reason for this was a lack of investments, as the government and ruling elite were amassing a larger portion of the shrinking mining revenues. Widespread strikes became common in the urban sectors of the economy.<sup>514</sup> The IMF-led austerity measures and wage freezes further exacerbated the grievances of the urban dwellers. The Zambian representative at the Fund's executive board, E. I. M. Mtei, implied that the failure of the SAP can be explained at least partially through this political dynamic:

“As a consequence, the stand-by arrangement had become inoperative earlier in the year, despite the Government's determined efforts to press ahead with major policy initiatives in the face of great opposition to further austerity from the strong and politically vocal workers' union.”<sup>515</sup>

To be sure, implementing the first real wave of liberalisation of the Zambian economy in 1983–1985 was a politically tough task for the UNIP government. The depreciation of

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<sup>511</sup> ZAMBIA – OVERDUE FINANCIAL OBLIGATIONS TO THE FUND – REPORT AND COMPLAINTS UNDER RULE K-1 AND RULE S-1 AND NOTICE OF FAILURE TO SETTLE TRUST FUND OBLIGATION, 6 . *EBM/85/180*, 7/31/1985. IMF Archives.

<sup>512</sup> ZAMBIA – OVERDUE FINANCIAL OBLIGATIONS – REPORT AND COMPLAINT UNDER RULE K-1 AND NOTICE OF FAILURE TO SETTLE TRUST FUND OBLIGATIONS, 19. *EBM/85/153-1 – Final*, 10/10/1985. IMF Archives.

<sup>513</sup> ZAMBIA – OVERDUE FINANCIAL OBLIGATIONS – REPORT AND COMPLAINTS UNDER RULE K-1 AND RULE S-1, AND NOTICE OF FAILURE TO SETTLE TRUST FUND OBLIGATIONS, 9–10. *EBM/85/132-2 – Final*, 11/4/1985. IMF Archives.

<sup>514</sup> Larmer 2010, 46–47; Rakner 2003, 59.

<sup>515</sup> ZAMBIA – OVERDUE FINANCIAL OBLIGATIONS – REPORT AND COMPLAINTS UNDER RULE K-1 AND RULE S-1, AND NOTICE OF FAILURE TO SETTLE TRUST FUND OBLIGATIONS, 9. *EBM/85/132-2 – Final*, 11/4/1985. IMF Archives.



the currency and high inflation were harshly felt in the pockets of ordinary Zambian people. In December 1982, five kwachas equalled approximately four dollars, but three years later six kwachas could buy only one dollar.<sup>516</sup> In November 1984, an on-off liberalisation of prices sent the cost of bread and wheat flour up by 80–90 per cent.<sup>517</sup>

In analysing the economic decline of Zambia in this period, bad timing seems to be a major factor once again. The global debt crisis prompted a change in the IFI's policies, but Zambia's debt problem had already matured long before that. The main target of the massive EFF loan in 1981 was the diversification of the Zambian economy, a reform that was already late and which the economy desperately needed. However, because of another copper price downturn, the EFF loan failed, and the emphasis in the Fund's policies switched markedly in 1982. Thus, in the aftermath of the eruption of the global debt crisis, the acute need to diversify the Zambian economy was postponed further. Instead, the focus was pinned on short-term liquidity and the repayment of existing debt. Because the copper prices remained low, the Zambian government could not achieve growth and fix the dire situation, despite its rather valiant efforts to implement the Fund's adjustment measures in 1983–1985.

This trajectory reflects neatly the narrative of growing US influence in the IFIs – especially in the Fund – during Reagan's first administration, outlined in the second chapter. Many of the Bank's former employees stressed that a major mistake in the IFI's policies was to follow the US lead in treating the debt crisis initially as a liquidity issue. In hindsight, this is exactly what happened in Zambia. Thus, it can be concluded that the 1983 SAP was the first one in Zambia, where the US influence seems to have played a significant part.

The performance criteria did not change much compared to earlier programs. Nevertheless, a significant change was witnessed in the content of the programs, again mirroring the American push for more comprehensive SAPs. During the previous decade, the programs had generally indicated policy areas that needed reforming, but specific measures were rarely included. While it is impossible to attribute the substance of every single small policy measure to the IFI staffs, in my opinion, the mere existence of very

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<sup>516</sup> ZAMBIA – REAL EFFECTIVE EXCHANGE RATE – INFORMATION NOTICE, 1–3. *EBIS/86/259*, 11/21/1986. IMF Archives.

<sup>517</sup> ZAMBIA – REVIEW UNDER STAND-BY ARRANGEMENT, 3. *EBM/84/169-2 – Final*, 11/26/1984. IMF Archives.

exact price and subsidy targets implies the Fund's push for detailed SAPs. Moreover, the micro-conditionality was accompanied by more extensive screening of the Zambian government's performance under the programs.

Moreover, earlier IFI documents portray the discussions with the Zambian officials as sincerely consultative processes. Although the IFIs still presented the SAPs of the 1980s as plans designed by the Zambian officials, the relationship had visibly transformed. As the Zambian government was verging on insolvency, the IFIs could more or less dictate the policy measures that had to be taken. In addition, the Zambian government was no longer responsible for formulating comprehensive long-term economic plans, as had been the case with the first and second national development plans. Instead, the Bank took a leading role in creating an investment program that spanned over several years.

In the Bank's case, tracing American influence behind its operations in Zambia is harder. As the second chapter of this study charted, the first half of the 1980s witnessed a struggle within the institution as the American influence was increasing. The US government wanted to assign distinct roles to the two institutions, but compared to the Bank, the Fund was enjoying the full American support at the time. The Bank had more trouble in securing additional funds, but on the other hand, it was leading the diversification efforts in Zambia more independently through the ZCG, because the Reagan administration's focus was on financial stabilisation.

The major change in the Bank during this period can be seen in the proliferation of neoliberal economic policies and the growing emphasis on structural adjustment. As a former employee of the Bank admitted in his interview, the 10 per cent cap on structural lending was circumvented by sectoral loans. This was exactly the case in Zambia, where the push for comprehensive structural adjustment was embedded in sector-specific loans. However, even if the diversification of the Zambian economy was recognised as the most important objective, the biggest loan of the period was nevertheless directed to the mining sector, because achieving short-term macroeconomic balance was seen as a prerequisite for economic growth. This was in line with the reasoning of the Fund and the US Treasury. In terms of results, the Bank's effort to diversify the Zambian economy was feeble.

The neoliberal influence is present in the Bank's operations of the time. The Bank and the Zambian officials had drawn up a plan that involved the gradual liberalisation of the state-planned economic model. In addition, the Bank was trying to promote private enterprises by reducing and streamlining the parastatal sector. To conclude, direct American influence is hard to detect in the Zambian case, but it is clear that at the same time the Bank was adopting a position that was similar to the Fund's and the US Treasury's stance. Drawing from the Zambian case it is evident that by the mid-1980s the neoliberal "purge" was complete at the Bank as managers like Anne Krueger had made their imprint on the institution.

### **3.5 The Pain of Adjustment: 1986–1991**

President Kaunda was a typical authoritarian leader at least in one manner: namely in that he persistently assigned the blame for Zambian hardships on external forces. Unfortunately, for a long time, the president had reasonable success in conveying his message to the people.<sup>518</sup> The most common explanations for the poor performance of the economy were the low copper prices and recurrent droughts.<sup>519</sup> This tactic diverted attention from the underlying problem, which was that the UNIP regime had allowed Zambian institutions to deteriorate and corruption to corrode economic management.<sup>520</sup> McPherson sums up the consequences by noting that "reform was postponed due to the general absence of accountability"<sup>521</sup>.

The last years of Kaunda's rule should be viewed against the backdrop of this failure. Eventually, the UNIP government's rule had to come to an end, because the prolonged economic disaster could not be solved by it. Richard Sandbrook has studied the role of states in implementing SAPs, and I find his conclusions to be illuminating in the Zambian context.<sup>522</sup> According to him, the thorough implementation of SAPs produces a paradox, because a strong state is needed to instigate reforms that are largely designed to diminish its own role in the economy:

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<sup>518</sup> McPherson 2004a, 41.

<sup>519</sup> McPherson 2004b, 308.

<sup>520</sup> McPherson 2004a, 43.

<sup>521</sup> McPherson 2004a, 41.

<sup>522</sup> Sandbrook 1991.

”Structural adjustment assumes an institutional capacity to design and implement complex policies concerning prices, trade, banking, finance and foreign investment, to reform parastatals, and to manage complicated negotiations with donors and the subsequent assistance programmes. The state, originally conceived as part of the problem of economic decline, is to contribute to the solution.”<sup>523</sup>

From this perspective, it is easy to see how the Zambian government was approaching a dead-end. In the last years of its existence, the UNIP government was facing a trade-off between the austerity and adjustment promoted by the IFIs, and the political considerations of the ruling elite. The Zambian people were increasingly opposed to the UNIP government, but simultaneously also against the austerity policies. This confrontation shaped the Zambian experience in the last years of the 1980s. A recent analogous example can be found in the struggles faced by Greece during the European debt crisis.<sup>524</sup>

Because of the decisiveness of this political dynamic, I intend to focus more on the political narrative in the last pages of this study. Analysing the Zambian economic situation in detail is not so relevant, because it is rather sufficient to point out that it was desperate. Moreover, tracing the American influence behind the last SAP after the 1991 elections is equally fruitless in my opinion, because it is evident that the program was largely shaped by the Washington Consensus. However, before recounting the path to the first free elections in more detail, it is essential to analyse the SAP from February 1986.

As the hopeless economic situation of Zambia unfolded in the summer of 1985, the Fund took on more extreme methods. At this point, it is safe to say that Zambia had lost its sovereignty in economic matters as the IFIs could more or less dictate the policies to be implemented. To begin with, the Fund introduced an auction-system to manage foreign exchange transactions. Due to its complicated nature, I will not specify the technical aspects of the system. It is adequate to note, that it was mainly designed to adjust the exchange rate towards the perceived market-value, which in reality meant a further depreciation of the kwacha. A Fund report concluded that the auction system “should be

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<sup>523</sup> Sandbrook 1991, 96.

<sup>524</sup> The case of Greece is interesting, because the EU and the European Central Bank (ECB) largely bypassed the Fund in handling the crisis. Although this can be partially explained by the risks associated with the single-currency, it implies that differential treatment is possible for certain countries. After all, turning to the Fund is the only viable option for most of the economically struggling developing countries of the world.

allowed to reflect to the maximum extent possible the influence of market forces”<sup>525</sup>. The auction system had immediate effects, as the value of the currency plummeted in April 1987 to 21 kwachas against one dollar.<sup>526</sup>

After the unsuccessful adjustment efforts of 1983–1985, new measures were introduced in order to insert a swift injection of liberalisation into the economy and unleash the forces of the private market. A host of supporting measures were introduced with the auction-system for achieving these targets: prices and interest rates were liberalised further, subsidies eliminated by most parts or completely, and trade regulation loosened.<sup>527</sup> The auction system and the supporting measures were meant to alleviate the acute liquidity and insolvency problems. In order to fix the economy in the longer term, a new SBA for two years (229.8 million SDR, plus an accompanying CFF-request worth 68.7 million) was agreed upon in February 1986.<sup>528</sup> The SAP followed the path of the previous ones, as the Fund staff still highlighted the acute need of financial stabilisation for achieving the longer term goals of growth and diversification.<sup>529</sup>

The novel element of the SAP was stressing the power of free markets more forcefully. In evaluating the auction system and other liberalising measures, the Fund report noted that they “represented a fundamental shift away from a relatively regulated economic system and toward an outward-looking, market-oriented policy environment”<sup>530</sup>. Besides its central aim of further liberalising the economy, the SAP included harsh austerity and heavy cuts on public spending. In addition to wage freezes and limits to personal emoluments, the public sector was slashed by cutting workforce, fast-tracking retirement and prohibiting new recruitment.<sup>531</sup>

Overall, the 1986 SAP was very comprehensive and rich in detail. Altogether 51 different policy measures and conditions can be found in a summary of the program’s elements, attached to the Appendix of the Fund report. The different elements of the program were extremely wide-ranging, as they included for example the elimination of the import

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<sup>525</sup> ZAMBIA – STAFF REPORT FOR THE 1985 ARTICLE IV CONSULTATION, 24. *SM/85/273*, 10/1/1985. IMF Archives.

<sup>526</sup> Meijer 1990, 669.

<sup>527</sup> Rakner 2003, 57; Meijer 1990, 69.

<sup>528</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 2. *EBS/86/24*, 2/3/1986. IMF Archives.

<sup>529</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 11. *EBS/86/24*, 2/3/1986. IMF Archives.

<sup>530</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 11. *EBS/86/24*, 2/3/1986. IMF Archives.

<sup>531</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 23. *EBS/86/24*, 2/3/1986. IMF Archives.

prohibition covering over 50 items; cutting maize and fertilizer subsidies by two thirds; organising an independent evaluation of the Zambia Airways' operations in order to streamline it; and permitting free collective bargaining.<sup>532</sup> The performance of the Zambian government was to be reviewed three times during the first year, and the last condition simply stated that "the completion of these reviews will constitute performance criteria"<sup>533</sup>.

The imprint of US authority – and the Baker Plan more specifically – is clearly visible in the SAP of 1986. A stress on market-oriented solutions had already surfaced in the introduction of the auction system, and this was followed enthusiastically in the SAP. The privatisation of the parastatal companies was not yet on the Fund's short-term agenda, although one target of the program was "to ensure that the enterprises are self-reliant"<sup>534</sup>. Considerable debt relief in the form of rescheduling was seen as imperative for the success of the program, but writing off any debt was not yet an option.<sup>535</sup>

Another key element of the Baker Plan was to enhance the role of the multilateral development banks (MDBs) and this is reflected in Zambia's adjustment process as well. In May 1986, the Bank drafted a medium-term recovery plan, which was tied to the earlier SAP so that the Fund program's "quantitative framework forms the initial phase of the Bank-Fund joint medium-term scenario for Zambia"<sup>536</sup>. To support the plan, the Bank issued a 50-million-dollar recovery credit to the Zambian government.<sup>537</sup> Regarding the importance of market forces, the Bank had clearly adopted an approach similar to that of the Fund. The main rationale for the credit was to ensure that necessary imports could be secured in order to carry through the Fund's stabilisation measures: "through its support of ongoing and additional policy and institutional reforms in Zambia, particularly the foreign exchange auction, it would help ensure greater efficiency of the economy"<sup>538</sup>. Following in the path of the earlier rehabilitation loans, reforming the parastatal sector

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<sup>532</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 38–43. *EBS/86/24*, 2/3/1986. IMF Archives.

<sup>533</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 32. *EBS/86/24*, 2/3/1986. IMF Archives.

<sup>534</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 31. *EBS/86/24*, 2/3/1986. IMF Archives.

<sup>535</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 35. *EBS/86/24*, 2/3/1986. IMF Archives.

<sup>536</sup> World Bank 1986, 8. *Zambia – Recovery Program Project (English)*. World Bank Archives.

<sup>537</sup> World Bank 1986, 1. *Zambia – Recovery Program Project (English)*. World Bank Archives.

<sup>538</sup> World Bank 1986, 33. *Zambia – Recovery Program Project (English)*. World Bank Archives.

was a pivotal component in the joint medium-term plan. Moreover, privatisation was emerging as a viable policy option:

”The Industrial Development Corporation has engaged consultants under the Industrial Reorientation Project (Cr. 1630-ZA) to help improve the efficiency of enterprises under its control through the restructuring of phasing out of all or some of their activities. This would include privatization where possible.”<sup>539</sup>

The Baker Plan was a watershed in the collaboration of the IFIs in Zambia. The institutions had increased their co-operation in the previous few years, but from 1985 onwards the Zambian policy outline was prepared jointly with all three parties involved.<sup>540</sup> The co-operation was fully institutionalised with the adoption of the Policy Framework Papers (PFPs), of which the first one was drafted by the staffs of both institutions during the year 1986.

The first PFP sketched out the IFI’s common medium-term strategy for the Zambian economy. One area that the paper singled out for reform was the public sector, which was deemed to absorb too much from the state’s coffers: “the ultimate goal is to reduce employment in the civil service to an efficient level, which is expected to require reduction by about one third the number of temporary daily workers over a three-year period”<sup>541</sup>. Interestingly, the PCP acknowledged that the medium-term strategy could have adverse effects on welfare in the short-term, but highlighted that “since a large proportion of the poor live in rural areas, the reduction in discrimination against agriculture and the rural sector inherent in the program should have definite distributional benefits”<sup>542</sup>.

To conclude, from late 1985 to early 1987 the IFIs were in charge of managing the economic situation of Zambia. The institutions worked closely together with the shared aim of thoroughly reforming the economy. Following the neoliberal approach to economic policy making, this was to be done by a host of measures, of which the most important were further liberalisation of prices and subsidies; streamlining or privatising

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<sup>539</sup> World Bank 1986, 17. *Zambia – Recovery Program Project (English)*. World Bank Archives.

<sup>540</sup> ZAMBIA – REQUEST FOR STAND-BY ARRANGEMENT, 1, 5. *EBS/86/24, 2/3/1986*. IMF Archives.

<sup>541</sup> ZAMBIA – MEDIUM-TERM ECONOMIC AND FINANCIAL POLICY FRAMEWORK, 7. *EBS/87/11, 1/22/1987*. IMF Archives.

<sup>542</sup> ZAMBIA – MEDIUM-TERM ECONOMIC AND FINANCIAL POLICY FRAMEWORK, 12. *EBS/87/11, 1/22/1987*. IMF Archives.

parastatal enterprises; and enforcing strict austerity in public finances, especially by cutting the size of the public sector.

The Baker Plan was later held as a turning point in the US government's stance towards the debt crisis, as it started to recognise the underlying structural problems holding back the developing countries. This does not, however, reflect itself in the 1986 SAP of Zambia, where the focus was still very much on financial stabilisation with an increased emphasis on the market-oriented neoliberal approach. The Fund created the Structural Adjustment Facility (SAF) in 1986, which had a medium-term outlook, but in many ways it came too late for Zambia. The economy was already in an acute state, and even more crucial were the political tensions that followed in 1987–1991, which would have made a comprehensive structural adjustment under the SAF (ESAF since 1987) impossible.

The political drama commenced in May 1987, when President Kaunda suddenly cut ties with the IFIs and terminated the SAP. Moreover, in a fiery speech, he accused the "neo-colonial" IFIs for bringing about Zambia's economic woes. Margaret Hanson and James Hentz have studied the ownership and spread of neoliberal policies in Africa. According to them, Kaunda's allegations were aimed at listeners both home and abroad.<sup>543</sup> Hanson and Hentz argue that the "financial coercion" exerted by the IFIs does not explain satisfactorily the probability of a state embracing neoliberal policies. Instead, the key variable in adopting them has been domestic political situations and more specifically electoral cycles.<sup>544</sup> Therefore, accounts that portray the spread of neoliberalism as influenced only by a one-sided push on the behalf of the IFIs should be viewed critically. Although ideological opposition to the IFIs (often framed as a critique of their neo-colonial meddling) has been common in Africa, it is often used in arguments spelled out in domestic political tussles for power.<sup>545</sup>

Indeed, the domestic political situation largely explains the UNIP government's actions. The harsh austerity of the effectual SAP had sparked unrest in the Copperbelt and Lusaka. In December 1986, 15 people died in food riots, which followed the decontrol of maize prices.<sup>546</sup> It has to be remembered that, despite Kaunda's authoritarian conduct, violent outbreaks were uncommon in Zambia, a rarity on the African continent as a whole.

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<sup>543</sup> Hanson & Hentz, 1999, 482–483.

<sup>544</sup> Hansin & Hentz, 1999, 480.

<sup>545</sup> Hanson & Hentz 1999, 480–481.

<sup>546</sup> Rakner 2003, 59.



However, considering the austerity measures, growing unemployment and rocketing inflation, it is not surprising that people took their protests to the streets. As the political situation was spiralling out of control, Kaunda decided to discard the IFIs in a move that was surely motivated more by his own chances of survival as the head of the state. Lise Rakner points out perceptively that the reasonable effort to stabilise the economy in 1983–1985 was preceded by elections (not the competitive sort), after which Kaunda was nevertheless able to consolidate his power.<sup>547</sup>

Following the break-up, President Kaunda introduced the New Economic Recovery Program (NERP), which was in essence a step back towards a model of state planning.<sup>548</sup> The kwacha was revalued significantly and debt repayment reduced.<sup>549</sup> The NERP should be viewed as a last desperate attempt of the Zambian government to hold on to what remained of its economic self-governance. Predictably, the experiment did not last very long, although Zambia did actually record some decent growth under the NERP in 1987–1988, mainly because of an excellent harvest.<sup>550</sup> However, breaking off the ties with the IFIs had drastic consequences, as no other donors were willing to lend to Zambia anymore and aid that had been negotiated earlier stopped rolling in. Kaunda had to retreat and talks about a new SAP were quietly started in the spring of 1989.<sup>551</sup>

At the time of the 1986 food riots, Chiluba – speaking as the leader of the trade unions – condemned the Fund for imposing monetarist policies on the “socialist” state of Zambia. The turmoil and Kaunda’s decision to cut ties with the IFIs exposed the UNIP government’s weakness and encouraged the opposition to get organised. The summer of 1990 was even more turbulent as more rioting and a failed coup shook the country. The unrest and mass protests emboldened the opposition further and Chiluba started to demand for more profound changes. Under the piling political pressure, Kaunda conceded and scheduled multi-party elections for October the next year.<sup>552</sup>

By the time of the elections, Chiluba had made a complete turnaround and MMD “was elected on a platform built on neoliberal policies”<sup>553</sup>. Hanson and Hentz maintain that this

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<sup>547</sup> Rakner 2003, 58.

<sup>548</sup> Kayizzi-Mugerwa 1991, 854.

<sup>549</sup> Rakner 2003 61–62.

<sup>550</sup> Hanson & Hentz 1999, 485.

<sup>551</sup> Rakner 2003, 61–62.

<sup>552</sup> Larmer 2010, 47.

<sup>553</sup> Hanson & Hentz 1999, 483.

change of mind was chiefly a political move, as the MMD framed its opposition now fully against Kaunda. The tactic worked, as MMD recorded a crushing victory in the parliamentary and presidential elections: the party took 125 seats in the parliament from a total of 150, and Chiluba won the presidency by taking 75 per cent of the popular vote.<sup>554</sup> Judging by the election result, Zambian people had increasingly turned against Kaunda and the political system, not just the austerity policies of the IFIs. Thus, Chiluba's political success was crucial in the adoption of neoliberal policies, and in my opinion, reaffirms Hanson's and Hentz' argument on the importance of domestic political currents.

The free and fair elections drew a lot of international attention as they were, unfortunately, quite exceptional at the time in Africa. This was reflected in the significant amounts of aid that started pouring in after the ballot.<sup>555</sup> Chiluba had campaigned by promising to liberalise the economy with policies that were later portrayed as "too aggressive for even the IMF's tastes"<sup>556</sup>. For the IFIs, however, this was welcome news, as the election result and MMDs commitment to reform finally offered a clean slate to start reorganising the whole economy. Thus, the liberalisation that started after the elections was reminiscent of what Naomi Klein has labelled the "shock treatment" of an economy, where old structures are overhauled swiftly in a wave of neoliberal policies.<sup>557</sup> To be sure, the spirit of the Washington Consensus was embodied in the very first paragraphs of the third PFP, which covered the essentials of the liberalisation process:

"The economic strategy recognizes the importance of market forces and reflects the conviction that Government should not undertake what the private sector can do at least as well. It is grounded in the view that individual initiative and freedom in the market place and in the political arena are essential for a thriving economy and a responsive political system. These beliefs are fortified by the conviction that free markets reinforce political freedoms, and vice versa."<sup>558</sup>

The Bank had initiated some new projects in the years 1986–1987, but after the rift with the Zambian government the lending ceased completely.<sup>559</sup> Through the 1980s, the Bank's inputs to Zambia had been smaller than the Fund's, but in the new decade the parts changed over as the Bank took a principal role in guiding the MDD government

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<sup>554</sup> Rakner 2003, 64.

<sup>555</sup> Hanson & Hentz 1999, 488.

<sup>556</sup> Hanson & Hentz 1999, 483. Quoted from the authors' interview, Bank of Zambia, 6 December 1995, Lusaka, Zambia.

<sup>557</sup> Klein 2008.

<sup>558</sup> Zambia – Economic and Financial Policy Framework 1992–94, 1. *EBD/92/32*, 2/27/1992. IMF Archives.

<sup>559</sup> World Bank website, 4 April 2019. *Where We Work / Zambia / All Projects*.

through the adjustment process. The Bank issued nearly 1.4 billion dollars to Zambia in 1991–1996. The loans were aimed to assist Zambia through the transformation in a comprehensive way: in achieving a macroeconomic balance in the economy; in investing in the diversification of the productive base; in assisting in the privatisation of state-owned companies; and more traditionally, in providing inputs to agriculture, health care and education.<sup>560</sup> With the Fund, the newly-elected Zambian government negotiated a three-year rights of accumulation program (RAP) in July 1992. The RAP was a novel type of agreement, where, by adhering to the SAP, the Zambian authorities acquired back the rights to draw capital again from the Fund in the future.<sup>561</sup>

The social consequences of the structural adjustment were devastating. Real GDP per capita fell to an all-time low of just over 900 dollars in 1994.<sup>562</sup> By 1993, the price of maize had risen 500 per cent and 20 000 public sector workers had lost their jobs.<sup>563</sup> The heavy burden of adjustment was distributed unevenly, as women and children suffered more because of cuts in health care and education. In addition, many of the subsistence farmers who lost rights to their land due to privatisation were women. Malnutrition increased child mortality and abandonment.<sup>564</sup> To compound the hardships, bad timing played a significant part again, as has been the case throughout the postcolonial history of Zambia. The country was hit by a devastating drought in 1991–1992.

An important aspect in the critique of the SAPs has been the questioning of some of the research on which the policies were based. Deborah Potts has studied the movement of people between urban and rural areas in Africa, and according to her, the IFIs did not fathom migration processes correctly in the 1980s. Potts argues that, after the debt crisis hit Africa, migration flows reversed from urban to rural in many countries. Moreover, cyclical migration became common as living standards worsened and opportunities were scarce both in urban and rural areas.<sup>565</sup>

The IFI's policies in Africa in the 1980s were influenced by two important studies, both dating to 1981. A Bank-report by Alan Berg highlights the persistent urban-rural income gap and rapid rate of urbanisation in the developing world. In his book *Markets and States*

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<sup>560</sup> World Bank website, 4 April 2019. *Where We Work / Zambia / All Projects*.

<sup>561</sup> Zambia – Accumulation of Rights, *EBS/92/114, Sup. 2, 7/28/1992*. IMF Archives.

<sup>562</sup> World Bank Open Data, 15 April 2019. *GDP per capita (constant 2010 US\$): Zambia*.

<sup>563</sup> Logie & Woodroffe, 43.

<sup>564</sup> Logie & Woodroffe, 42.

<sup>565</sup> Potts 1995, 259–260.

*in Tropical Africa: The Political Basis of Agricultural Policies*, Robert H. Bates in turn is critical of the prevalent agricultural marketing policies in developing countries at the time. Both studies emphasise the detrimental effects of subsidising basic commodities as they are seen to sustain urban middle-class consumption at the expense of rural subsistence farmers.<sup>566</sup>

Indeed, the fast rate of urbanisation and rural-urban wage gap are perpetual themes in the IFI documents treating Zambia in the 1970s and 1980s. A Bank report from 1981 asserted that, despite the growth rate of urban areas slowing down a bit since independence, “the absolute numbers involved are staggering”<sup>567</sup>. The Bank’s contemporary data reveal that rapid population growth facilitated a steady urban expansion through the 1980s, but the pace proved to be significantly slower than initially was projected. In fact, while 40 per cent of the population lived in urban areas in 1980, the percentage declined 0.5 points during the decade.<sup>568</sup> Potts has calculated that the Bank’s estimation of the rate of urbanisation was nearly 81 per cent too high back in 1980.<sup>569</sup> In this light, the misjudgement of the IFIs looks serious.

Potts claims that profound changes – missed largely by the IFIs – had already taken place in Zambia during the 1970s. The urban growth rate was extremely high from 1963 to 1969, and this trend was expected to continue. Bates had studied the post-independence urbanisation in Zambia and the government’s policies that he judged to contribute to sustaining an “urban bias”. His influential work in 1981 drew upon these earlier studies and thus continued to project fast urban growth. Potts argues, however, that migration flows adjusted to the long recession already in the 1970s.<sup>570</sup> Moreover, by the 1980s, the privileged position of the urban classes could be questioned. While an urban elite had been a common feature of African societies in the 1960s, the rural-urban income gap declined steadily during the next decade and trade unions lost their earlier strength. In the 1980s, there was no more a distinct urban class to speak of. The informal sector had grown and an influx of unskilled workers created several class layers in the urban population.<sup>571</sup>

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<sup>566</sup> Berg 1981; Bates 1981.

<sup>567</sup> World Bank 1981, 21. *Zambia – Country economic memorandum (English)*. World Bank Archives.

<sup>568</sup> World Bank Open Data, 20 March 2019. *Urban population (% of total): Zambia*.

<sup>569</sup> Potts 1995, 252.

<sup>570</sup> Potts 1995, 252.

<sup>571</sup> Potts 1995, 247–248.

A common feature of the SAPs of the 1980s in Africa was targeting urban consumption, especially through pricing policies and the elimination of subsidies. These adjustment policies hit the urban poor hard as the prices of basic foodstuffs and other vital commodities, such as petrol, rocketed. In Zambia, it resulted in increased poverty and child mortality.<sup>572</sup> In addition, the adjustments always included austerity in the public sector, which in effect meant slashing education, health care and transport.<sup>573</sup> Moreover, while the urban-rural wage gap may well have been still a significant issue back in 1981, the IFIs did not revise their view during the decade at all. Potts sums up the mistake: “yet the structural adjustment policies implemented since 1989 have taken no cognizance of this fact, and have been exceedingly harsh in trying to “correct” an imbalance which no longer existed”<sup>574</sup>.

Other studies have verified the “urban bias” miscalculation. An investigation by Allast M. Mwanza, Nkonga Mwamba and Eniwet Kakuwa shows that it was already well known by the time of their review in the early 1990s:

”By 1986, some 35 to 40% of urban households were living below the Poverty Datum Line. Evidence further indicated that the rural income gap had narrowed down whereas in urban areas, the rich-poor gap had widened. Moreover, the decline in urban incomes was accompanied by a massive contraction of formal sector employment.”<sup>575</sup>

The liberalisation of prices and elimination of subsidies were universal elements in the SAPs around the world. In many parts of the globe, the policies were directed at a perceived “labour aristocracy”<sup>576</sup>, as the actual make-up of urban classes was not thoroughly enough investigated. As a result, poor and unskilled workers of the informal sector were hit hardest by the adjustment policies. This process was exacerbated in Africa, due to a lack (and misreading) of data by the IFIs. Because of its early and rapid urbanisation, Zambia is one of the clearest examples of an African state, whose development has been affected by this largely illusive “urban bias”.

The years after the free elections were the toughest period in the postcolonial history of Zambia. The speedy recovery never arrived and the liberalisation of the economy proved to be a more protracted and socially arduous process than expected. The MMD

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<sup>572</sup> Potts 1995, 249.

<sup>573</sup> Potts 1995, 259–260.

<sup>574</sup> Potts 1995, 252.

<sup>575</sup> Mwanza, Mwamba & Kakuwa 1992, 136.

<sup>576</sup> Potts, 247.

government was partly at fault, as in many cases the implementation of the reforms was not done satisfactorily. Especially in his second stint in power from 1996 to 2001, Chiluba's eagerness to reform the economy diminished because staying in power became a more pressing priority.<sup>577</sup> After a promising start, the newly born Zambian democracy took steps backwards as the ruling class manipulated institutions and fostered corruption in governance.<sup>578</sup>

Zambia's prospects look better in the new millennia as the rising global demand for copper sparked an economic boom in the early 2000s. However, despite the robust economic growth of the past years, 54 per cent of Zambians are still poor at present times.<sup>579</sup> Crucially, the Zambian economy has become more diversified, making it less dependent on the mining sector, which still contributed 15.4 per cent of GDP in 2017.<sup>580</sup> On the troubling side, Zambian external debt has been mounting again after being largely written off under the HIPC program in 2005. The debt has climbed to 59 per cent of the GDP in the past ten years, with China holding a quarter of it. Even more worrying is the widespread corruption and movement towards authoritarianism that has accompanied the escalating indebtedness.<sup>581</sup>

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<sup>577</sup> Rakner 2003, ??? (70)?

<sup>578</sup> Rakner 2003, 186–188.

<sup>579</sup> African Development Bank Group (AfDB) website, 15 January 2019. *African Economic Outlook (AEO) 2018: Zambia*, 7.

<sup>580</sup> AfDB website, 15 January 2019. *African Economic Outlook (AEO) 2018: Zambia*, 3.

<sup>581</sup> The Economist, 15 September 2018.

## 4. Conclusions

The United States (US) played a pivotal role in creating the Structural Adjustment Programs (SAPs) of the 1980s and 1990s. The development of conditionality in the lending policies of the International Financial Institutions (IFIs) was a crucial part of this process, and this development was strongly influenced by the US from the very beginning. The Americans insisted on formulating certain open-ended paragraphs in the Fund's Articles of Agreement, and these enabled the later expansion of conditionality. After the Bretton Woods system broke down, a transitory period followed as the Fund had to reinvent its purpose to some extent. The US government contributed significantly to the Fund's metamorphosis as it pushed for increased conditionality in the organisation, which, in turn, enabled the institution to take on novel ventures. After the eruption of the debt crisis in 1982, an initially reluctant American government began to enhance the role of the Fund. Under US guidance, the Fund moved towards an increasing extent of microconditionality and issued constantly tightening and more wide-ranging SAPs throughout the 1980s.

Tracing neoliberal aspirations in the Fund's lending policies is not as straightforward a task. This is mainly due to the institution's primary concern in fixing balance of payments problems and other macroeconomic issues. To be sure, neoclassical economics guided the Fund's operations already in the 1970s. However, at that time, the Fund did not thoroughly and openly embrace the neoliberal agenda, which was centred around the mission of retasking the state in a comprehensive way in order to turn the "statist" developing countries into liberal market economies. Despite this, it must be concluded that the Fund did endorse the neoliberal policy program in the 1980s. After all, it did forge a close alliance with the US Treasury.

Conditionality developed at a later stage in the lending policies of the Bank, and the US did not have a central role in the process, as had been the case with the Fund. When decolonisation gained pace, the US was able to promote the Bank as the major global creditor for the developing world, in place of the more egalitarian and ideologically diverse United Nations (UN). After this, however, the US stepped back and the Bank

gained more autonomy under the leadership of Robert S. McNamara, who guided the institution toward a broader developmentalist agenda.

The US stance altered in the 1980s, mainly because of a change in administration with the Republican Ronald Reagan taking office. An ideological clash ensued in the Bank. In this battle, the neoliberal line of thought prevailed and critical voices were ousted or marginalised. The Americans played a part in this by influencing the recruitment of top management. After the introduction of the Baker Plan, the Bank was accepted as an equal member in the alliance that was already in place between the Fund and the US government. The closer cooperation between the IFIs was institutionalised with the adoption of the Policy Framework Papers (PFPs). By the last years of the decade, the Bank had adopted the neoliberal program completely, as the push to privatise state-owned companies, for example, testifies. Thus, the Bank became the third pillar of support for the Washington Consensus.

In my opinion, a sociological view in studying the IFIs is paramount for achieving a fruitful analysis. Too often, the institutions are presented as passive agents, easily led by outside pressure. It is true that, in most cases, it made sense for the IFIs to follow the lead of the US and other Western industrial countries. This is fairly understandable, because, unlike in the UN, power is linked to financial weight in the IFIs. In this respect the world has changed since the 1980s. The past years have seen the rise of China and other big emerging economies. In addition, a handful of the old industrial nations have formed a powerful economic and political block in the European Union (EU). Although the head of the Bank is still selected by the US president, the Bank has distanced itself from the US government and focused on issues like poverty reduction, sustainable development and gender equality. Likewise, the Fund has highlighted its impartial status since the days of the Washington Consensus.

The US influence and the neoliberal breakthrough in the IFIs are evident in the case of Zambia. In the first half of the 1970s, the Bank was very committed to Zambian development. The Bank assessed that the UNIP government was able to implement sound economic policies, and it did not oppose the nationalisations in the key sectors of the economy. Gradually, as the economic situation worsened in Zambia, the Bank's trust in the UNIP government waned. The Fund was marginalised by the US government in the 1970s. This meant that it had a freedom to operate, but, on the other hand, its stature in



the international financial markets was modest, and conditionality was still at a comparatively low level. The relative autonomy of the IFIs with regard to US influence did not benefit Zambia, quite the contrary. The cooperation between the institutions was inadequate as they had different, and somewhat conflicting, goals in the Zambian context. Moreover, both institutions kept issuing new loans to Zambia, although the country's debt was piling up and the UNIP government's performance in implementing the accompanying policy programs was questionable.

In the first years of the 1980s, the considerable changes that were taking place within the IFIs were reflected as rather inconsistent policies in Zambia. The Fund had a bigger role in the Zambian adjustment process in these years. The substantial Extended Fund Facility (EFF) loan was targeted at diversifying the Zambian economy, but it was doomed to fail because the copper price projections proved overly optimistic. After the debt crisis, the Fund's approach in Zambia changed as the institution's focus shifted to acute liquidity issues, following the general line of the US Treasury in handling the global emergency. The Bank was only beginning to adopt structural adjustment loans (SALs) in this period. In Zambia, the Bank experimented with sectoral program loans, which yielded disappointing results in terms of diversifying the economy. Although the cooperation of the IFIs was not yet formalised, the institutions started to work more closely together in these years. In addition, the IFIs had a major role in organising new funds and debt rescheduling for Zambia with other donors and financiers.

In the second half of the 1980s, US influence became very apparent in the case of Zambia. After the introduction of the Baker Plan, the IFIs started formulating policies for Zambia in complete collaboration. The emphasis was on fostering the free markets and achieving a comprehensive liberalisation of the "statist" economy. The IFIs had considerable leverage in decreeing policies, because Zambia was on the verge of default. The climax of US influence was witnessed in the 1991 SAP, two years after the Washington Consensus was forged. The adjustment was sorely needed due to the hopeless state of affairs in Zambia, and it laid the ground for later growth and diversification. In hindsight, however, the shock treatment of 1991 seems rather harsh since the IFI's approach changed soon after. Zambia was approved into the Heavily Indebted Poor Countries (HIPC) program in 1996 and its debt was completely wiped out ten years later.

The truly disheartening conclusion, which can be drawn from this study, is that the Zambian economic collapse was not unavoidable. First and foremost, the blame should be assigned to Zambia's government, which made several cumulative errors that were crucial in bringing about the disaster. The first mistake of the UNIP government was to postpone the diversification of the economy during the copper boom. The Zambian government adopted a strategy of appeasing urban laborers and public-sector workers, who constituted the core support of the UNIP party. As a result, the economy remained vulnerable to external shocks, and a culture of patronage was rooted in the important parastatal sector of the economy.

The second erroneous move was made in the aftermath of the copper price shock. Instead of adjusting the economy when it could have been done with relatively small sacrifices, the UNIP government borrowed from the deregulated international capital markets in order to sustain domestic consumption and finance budget deficits. The decision was motivated, at least partly, by the belief that the copper price slump would be brief. By the 1980s, the economic situation was beyond a quick fix. However, President Kenneth Kaunda and his party comrades did no favours to the Zambian people by clinging onto power and thus protracting the crisis. Corruption intensified in the process as larger portions of the shrinking export revenues were hoarded by the ruling elite. During these turbulent years, Zambia lost its position as a middle-income country and large parts of the rapidly growing population were dragged into poverty. Informal employment became common and new classes of urban poor emerged.

While it would be extremely unfair to blame the IFIs for the Zambian hardships, it can be concluded, that the institutions were not very successful in helping the country. One could argue, that the task was impossible due to the mismanagement of the Zambian government. In my opinion, however, this claim is not a sufficient explanation alone. It is important to note that the Zambian economy was dragged into trouble because of external shocks. From this perspective, it would be reasonable to expect better assistance from the institutions that were designed to provide support precisely in these circumstances.

Moreover, the troubles in Zambia should be viewed against the larger context of a changing external economic environment. "The rules of the game" in the global economy were rewritten after the Bretton Woods system collapsed, but countries like Zambia had

no part in this process. It can be argued that the profound changes were mostly beyond control, but at least the Western powers – due to their hegemony in the system and their influence in the IFIs – were able to manage the transition better. In contrast, Zambia's position, as an open and undiversified economy on the periphery, was a very exposed one. Zambia is dependent on the production of a single raw material and a "price taker" in the global economy, as the value of copper is dictated in the London Metal Exchange. The extremely vulnerable economic position is made even more precarious by Zambia's location as a land-locked country. Ten years after gaining independence, the country found itself in a very unstable part of the world. Zambia's economic troubles were aggravated because the state was slow to adapt to the external changes. Under the leadership of President Kaunda, the country tried to hold onto the model of state control, which was rapidly becoming outdated. However, this investigation has shown that the IFIs were also sluggish in adapting to the changing external environment.

Therefore, an important aspect to be learned from this study is the significant role of timing in the process of adapting to neoliberal policies. Too often, the SAPs around the world are treated as fairly identical processes, when in fact complete narratives about the impacts of the programs require a thorough understanding of the gradual transformation of the IFIs (affected largely by US influence) on the one hand, and domestic political dynamics on the other. In the Zambian case, the adjustment process stretched over a long period. It was one of the first countries to accumulate significant amounts of debt after the oil crisis. In spite of the protracted process of adjustment, the decisive blow was nevertheless sharp. Because of the continually failed efforts to adjust the economy and the political deadlock of the 1980s, the final phase of adjustment took the form of a shock blow to the economy.

Irrespective of the precise time of adjustment, the SAPs did have common characteristics around the world. The most obvious shared feature was the hard social consequences of adjustment. SAPs in Latin America, Africa and Eastern Europe all increased income differences and hurt segments of society that were already disadvantaged. These outcomes can be largely attributed to the neoliberal content of the policies, but in the Zambian case the situation was aggravated by the IFI's misjudgement of the rural-urban migration patterns. The positive aspect in the Zambian case was the relatively peaceful democratic transition that accompanied the liberalisation process. The free elections gave

a credible mandate for Frederick Chiluba to reform the economy, although unfortunately, the reign of the former trade union boss proved to be disappointing and characterised by wide-spread corruption.

The Zambian experience highlights the importance of sound domestic institutions. The successful implementation of SAPs requires an active state, but I would argue that democratic and transparent institutions constitute a second precondition. Substantial economic reforms are hard to execute without an active civil society and functioning economic and political institutions. However, it is equally important to maintain transparency within the global multilateral institutions. In fact, this study has exposed some of the dangers associated with multilateral institutions that are operating under external pressure. Moreover, developments in the past years have highlighted the need for strong independent multilateral institutions, as bilateral lenders like China have emerged as sources of cheap credit in Africa.

It has been clear to me from the very beginning that this study will not produce a straightforward set of conclusions. The goal of the study was to offer a nuanced analysis, and in this respect, I believe it has served its purpose. At least I have been able to clarify my own thoughts in relation to a topic that initially seemed incredibly complicated and disputed. The relational approach has been essential to this process. By pinpointing the focus on two distinct questions and their interaction, I have gained insights into the wider dynamics of the complex set of relations that have shaped the debt crisis in Africa. I believe that this study can pave the way for additional research. It would be interesting to apply the same approach in a comparative analysis of the implementation of SAPs in different parts of the world.

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## List of Abbreviations

<b>AAC</b>	Anglo American Corporation
<b>AfDB</b>	African Development Bank
<b>ANC</b>	African National Congress of Northern Rhodesia
<b>AsDB</b>	Asian Development Bank
<b>BoZ</b>	Bank of Zambia
<b>BSAC</b>	British South Africa Company
<b>CAF</b>	Central African Federation
<b>CEMLA</b>	Centre for Latin American Monetary Studies
<b>CFF</b>	Compensatory Financing Facility
<b>CIPEC</b>	Council of Copper Exporting Countries
<b>EBRD</b>	European Bank for Reconstruction and Development
<b>ECB</b>	European Central Bank
<b>EEC</b>	European Economic Community
<b>EFF</b>	Extended Fund Facility
<b>ESAF</b>	Enhanced Structural Adjustment Facility
<b>EU</b>	European Union
<b>Fed</b>	Federal Reserve
<b>G7</b>	Group of Seven
<b>G10</b>	Group of Ten
<b>GDP</b>	gross domestic product
<b>GNI</b>	gross national income
<b>GS</b>	genuine savings
<b>IBRD</b>	International Bank of Reconstruction and Development
<b>ICSID</b>	International Centre for Settlement of Investment Disputes
<b>IDA</b>	International Development Association
<b>IDB</b>	Inter-American Development Bank
<b>IFC</b>	International Finance Corporation
<b>IFIs</b>	international financial institutions
<b>IMF</b>	International Monetary Fund
<b>HIPC</b>	Heavily Indebted Poor Countries

<b>MDBs</b>	multilateral development banks
<b>MMD</b>	Movement for Multi-Party Democracy
<b>NAM</b>	Non-Aligned Movement
<b>NAMBOARD</b>	National Agricultural Marketing Board
<b>NCCM</b>	Nchanga Consolidated Copper Mines
<b>NERP</b>	New Economic Recovery Program
<b>OAPEC</b>	Organisation of Arab Petroleum Exporting Countries
<b>OPEC</b>	Organisation of Petroleum Exporting Countries
<b>PFPs</b>	Policy Framework Papers
<b>PRGF</b>	Poverty Reduction and Growth Facility
<b>RAP</b>	rights of accumulation program
<b>RCM</b>	Roan Consolidated Mines
<b>RST</b>	Rhodes Selection Trust
<b>SAF</b>	Structural Adjustment Facility
<b>SAL</b>	structural adjustment loan
<b>SAP</b>	structural adjustment program
<b>SBA</b>	Stand-by Arrangement
<b>SDR</b>	Special Drawing Right
<b>SUNFED</b>	Special United Nations Fund for Economic Development
<b>TAZARA</b>	Tanzania-Zambia Railway
<b>UDI</b>	Unilateral Declaration of Independence
<b>UK</b>	United Kingdom
<b>UN</b>	United Nations
<b>UNCTAD</b>	United Nations Conference on Trade and Development
<b>UNFPA</b>	United Nations Population Fund
<b>UNIP</b>	United National Independence Party
<b>UPP</b>	United Progressive Party
<b>US</b>	United States
<b>ZCCM</b>	Zambia Consolidated Copper Mines
<b>ZCG</b>	Zambia Consultative Group